

# **Chung Hung Steel Corporation**

**Financial Statements for the  
Years Ended December 31, 2012 and 2011 and  
Independent Auditors' Report**

## INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders  
Chung Hung Steel Corporation

We have audited the accompanying balance sheets of Chung Hung Steel Corporation (the "Corporation") as of December 31, 2012 and 2011, and the related statements of income, changes in stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the Rules Governing the Audit of Financial Statements by Certified Public Accountants and auditing standards generally accepted in the Republic of China (ROC). Those rules and standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of Chung Hung Steel Corporation as of December 31, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, requirements of the Business Accounting Law and Guidelines Governing Business Accounting relevant to financial accounting standards, and accounting principles generally accepted in the ROC.

March 18, 2013

### Notice to Readers

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

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

**CHUNG HUNG STEEL CORPORATION**

**BALANCE SHEETS**

**DECEMBER 31, 2012 AND 2011**

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

ASSETS	2012		2011		LIABILITIES AND STOCKHOLDERS' EQUITY	2012		2011	
	Amount	%	Amount	%		Amount	%	Amount	%
<b>CURRENT ASSETS</b>					<b>CURRENT LIABILITIES</b>				
Cash	\$ 59,131	-	\$ 89,167	-	Short-term loans (Notes 12 and 24)	\$ 8,219,221	24	\$ 12,836,560	36
Financial assets at fair value through profit or loss (Notes 2 and 4)	3,164	-	4,586	-	Commercial paper payable (Note 13)	1,668,795	5	1,549,300	4
Accounts receivable (Notes 2, 3 and 5)	1,105,675	3	751,335	2	Financial liabilities at fair value through profit or loss (Notes 2 and 4)	3,737	-	-	-
Accounts receivable from related parties (Note 23)	15,472	-	186,517	1	Notes payable (Note 23)	27,176	-	-	-
Other receivables	21,021	-	79,720	-	Accounts payable	1,204,519	4	1,125,426	3
Other receivables from related parties (Note 23)	178,522	-	44,412	-	Accounts payable to related parties (Note 23)	243,927	1	136,458	-
Inventories (Notes 2 and 6)	6,631,860	20	8,793,195	24	Accrued expenses (Notes 15 and 23)	447,827	1	388,331	1
Prepayments	942,877	3	846,987	2	Other payables (Notes 16 and 23)	347,543	1	321,281	1
Restricted assets (Note 24)	300,000	1	300,000	1	Current portion of long-term loans (Notes 14 and 24)	1,076,923	3	-	-
Others (Note 23)	69,815	-	199,909	1	Others (Notes 2 and 25)	46,416	-	647,438	2
Total current assets	9,327,537	27	11,295,828	31	Total current liabilities	13,286,084	39	17,004,794	47
<b>INVESTMENTS (Notes 2, 4, 7, 8 and 9)</b>					<b>LONG-TERM LIABILITIES</b>				
Investments accounted for by the equity method	4,996,845	15	5,209,889	15	Financial liabilities at fair value through profit or loss (Notes 2 and 4)	1,739	-	-	-
Financial asset at fair value through profit or loss	259	-	23,979	-	Long-term loans, net of current portion (Notes 14 and 24)	10,379,115	31	5,338,336	15
Available-for-sale financial assets	1,161,753	3	1,205,266	3	Total long-term liabilities	10,380,854	31	5,338,336	15
Financial assets carried at cost	285,625	1	290,635	1	<b>RESERVES</b>				
Total investments	6,444,482	19	6,729,769	19	Reserve for land value increment tax (Note 10)	144,434	1	144,434	-
<b>PROPERTIES (Notes 2, 10, 23, 24 and 25)</b>					<b>OTHER LIABILITIES</b>				
Land	2,886,801	9	2,886,080	8	Accrued pension cost (Note 17)	125,984	-	134,027	-
Buildings and improvements	2,674,014	8	2,500,427	7	Guarantee deposits received (Note 11)	35,000	-	35,000	-
Machinery and equipment	16,383,560	49	16,081,278	44	Deferred credits (Notes 2 and 23)	986,702	3	1,068,844	3
Spare parts	1,363,028	4	1,354,042	4	Total other liabilities	1,147,686	3	1,237,871	3
Other equipment	3,514,262	10	3,452,078	9	Total liabilities	24,959,058	74	23,725,435	65
Total costs	26,821,665	80	26,273,905	72	<b>STOCKHOLDERS' EQUITY</b>				
Revaluation increment	331,820	1	331,820	1	Common stock - NT\$10.00 par value; authorized - 2,043,160 thousand shares; issued and outstanding - 1,435,544 thousand shares (Note 18)	14,355,444	42	14,355,444	40
Cost and revaluation increment	27,153,485	81	26,605,725	73	Capital surplus (Note 18)	342,910	1	342,955	1
Less: Accumulated depreciation	14,835,702	44	13,420,474	37	Accumulated deficit (Note 18)	-	-	154,487	1
	12,317,783	37	13,185,251	36	Legal reserve	-	-	-	-
Construction in progress	758,262	2	616,883	2	Accumulated deficit	(5,756,591)	(17)	(2,437,867)	(7)
Prepayments for equipment	756,492	2	167,224	-	Accumulated deficit	(5,756,591)	(17)	(2,283,380)	(6)
Net properties	13,832,537	41	13,969,358	38	Other equity (Notes 10 and 18)				
<b>OTHER ASSETS (Notes 2 and 11)</b>					Unrealized revaluation increment	356,897	1	356,897	1
Assets leased to others	2,726,380	8	2,726,924	8	Unrealized loss on financial instruments	(395,863)	(1)	(244,813)	(1)
Nonoperating assets, net	1,441,942	5	1,441,942	4	Total other equity	(38,966)	-	112,084	-
Refundable deposits	22,224	-	21,894	-	Total stockholders' equity	8,902,797	26	12,527,103	35
Others	66,753	-	66,823	-	<b>TOTAL</b>	<b>\$ 33,861,855</b>	<b>100</b>	<b>\$ 36,252,538</b>	<b>100</b>
Total other assets	4,257,299	13	4,257,583	12					
<b>TOTAL</b>	<b>\$ 33,861,855</b>	<b>100</b>	<b>\$ 36,252,538</b>	<b>100</b>					

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

# CHUNG HUNG STEEL CORPORATION

## STATEMENTS OF INCOME YEARS ENDED DECEMBER 31, 2012 AND 2011 (In Thousands of New Taiwan Dollars, Except Loss Per Share)

	2012		2011	
	Amount	%	Amount	%
SALES (Notes 2 and 23)	\$ 43,933,002	105	\$ 47,009,819	103
LESS: SALES RETURNS AND ALLOWANCES	<u>1,901,742</u>	<u>5</u>	<u>1,513,360</u>	<u>3</u>
NET SALES	42,031,260	100	45,496,459	100
SERVICE REVENUE	95,267	1	124,805	1
OTHER OPERATING REVENUE	<u>31,954</u>	<u>-</u>	<u>13,465</u>	<u>-</u>
TOTAL OPERATING REVENUE	42,158,481	101	45,634,729	101
OPERATING COSTS (Notes 6, 20 and 23)	<u>44,453,233</u>	<u>106</u>	<u>47,699,715</u>	<u>105</u>
GROSS LOSS	<u>(2,294,752)</u>	<u>(5)</u>	<u>(2,064,986)</u>	<u>(4)</u>
OPERATING EXPENSES (Notes 20 and 23)				
Selling	876,382	2	912,290	2
General and administrative	<u>215,752</u>	<u>1</u>	<u>249,236</u>	<u>1</u>
Total operating expenses	<u>1,092,134</u>	<u>3</u>	<u>1,161,526</u>	<u>3</u>
OPERATING LOSS	<u>(3,386,886)</u>	<u>(8)</u>	<u>(3,226,512)</u>	<u>(7)</u>
NONOPERATING INCOME AND GAINS				
Interest income	1,383	-	1,377	-
Investment income recognized under the equity method, net (Note 9)	-	-	121,907	-
Dividend income	43,118	-	108,645	-
Exchange gain, net	81,886	-	91,008	-
Rent revenue (Notes 11 and 20)	67,514	-	51,180	-
Reversal of impairment loss, net (Note 11)	-	-	346,971	1
Others (Notes 4 and 23)	<u>118,332</u>	<u>1</u>	<u>233,290</u>	<u>1</u>
Total nonoperating income and gains	<u>312,233</u>	<u>1</u>	<u>954,378</u>	<u>2</u>
NONOPERATING EXPENSES AND LOSSES				
Interest expense (Note 10)	252,754	1	158,381	-
Investment loss recognized under the equity method (Note 9)	100,262	-	-	-
Losses on sale of fixed assets	22,339	-	783	-
Others (Note 4)	<u>23,263</u>	<u>-</u>	<u>8,388</u>	<u>-</u>
Total nonoperating expenses and losses	<u>398,618</u>	<u>1</u>	<u>167,552</u>	<u>-</u>

(Continued)

# CHUNG HUNG STEEL CORPORATION

## STATEMENTS OF INCOME

YEARS ENDED DECEMBER 31, 2012 AND 2011

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

	2012		2011	
	Amount	%	Amount	%
LOSS BEFORE INCOME TAX	\$ (3,473,271)	(8)	\$ (2,439,686)	(5)
INCOME TAX EXPENSE (BENEFIT) (Notes 2 and 19)	(60)	-	8,230	-
NET LOSS	<u>\$ (3,473,211)</u>	<u>(8)</u>	<u>\$ (2,447,916)</u>	<u>(5)</u>
	2012		2011	
	Before Income Tax	After Income Tax	Before Income Tax	After Income Tax
LOSS PER SHARE (Note 21) Basic	<u>\$ (2.42)</u>	<u>\$ (2.42)</u>	<u>\$ (1.70)</u>	<u>\$ (1.71)</u>

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

(Concluded)

**CHUNG HUNG STEEL CORPORATION**

**STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
YEARS ENDED DECEMBER 31, 2012 AND 2011  
(In Thousands of New Taiwan Dollars)**

	Issued and Outstanding Common Stock	Capital Surplus	Retained Earnings (Accumulated Deficit)			Other Equity		Total Stockholders' Equity
			Legal Reserve	Unappropriated Earnings (Deficit)	Net	Unrealized Revaluation Increment	Unrealized Gain (Loss) on Financial Instruments	
BALANCE, JANUARY 1, 2011	\$ 13,803,312	\$ 344,201	\$ -	\$ 1,544,867	\$ 1,544,867	\$ -	\$ 207,163	\$ 15,899,543
Appropriations of 2010 earnings (Note 18)								
Legal reserve	-	-	154,487	(154,487)	-	-	-	-
Cash dividends - 6%	-	-	-	(828,199)	(828,199)	-	-	(828,199)
Stock dividends - 4%	552,132	-	-	(552,132)	(552,132)	-	-	-
Compensation cost of exercised stock options issued by the parent company	-	160	-	-	-	-	-	160
Change in unrealized loss on available-for-sale financial assets	-	-	-	-	-	-	(129,933)	(129,933)
Adjustment from changes in equity recognized under the equity method	-	(1,406)	-	-	-	169,511	(322,043)	(153,938)
Change in unrealized revaluation increment	-	-	-	-	-	187,386	-	187,386
Net loss in 2011	-	-	-	(2,447,916)	(2,447,916)	-	-	(2,447,916)
BALANCE, DECEMBER 31, 2011	14,355,444	342,955	154,487	(2,437,867)	(2,283,380)	356,897	(244,813)	12,527,103
Legal reserve used to offset deficit (Note 18)	-	-	(154,487)	154,487	-	-	-	-
Change in unrealized loss on available-for-sale financial assets	-	-	-	-	-	-	(43,513)	(43,513)
Adjustment from changes in equity recognized under the equity method	-	(45)	-	-	-	-	(107,537)	(107,582)
Net loss in 2012	-	-	-	(3,473,211)	(3,473,211)	-	-	(3,473,211)
BALANCE, DECEMBER 31, 2012	<u>\$ 14,355,444</u>	<u>\$ 342,910</u>	<u>\$ -</u>	<u>\$ (5,756,591)</u>	<u>\$ (5,756,591)</u>	<u>\$ 356,897</u>	<u>\$ (395,863)</u>	<u>\$ 8,902,797</u>

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

# CHUNG HUNG STEEL CORPORATION

## STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2012 AND 2011 (In Thousands of New Taiwan Dollars)

	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net loss	\$ (3,473,211)	\$ (2,447,916)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation	1,604,659	1,559,053
Amortization	-	7,030
Compensation cost of exercised stock options issued by the parent company	-	160
Allowance for loss on inventories	259,945	1,129,124
Investment loss (income) recognized under the equity method, net	100,262	(121,907)
Cash dividends received from equity - method investments	5,200	3,900
Loss on disposal of properties	22,339	783
Valuation loss (gain) on financial instruments	17,686	(28,284)
Reversal of impairment loss on properties	-	(346,971)
Realized gain on disposal of collaterals of nonperforming loans	(82,142)	(82,143)
Purchase contract loss	846,325	1,579,220
Others	9,188	3,400
Net changes in operating assets and liabilities		
Financial assets at fair value through profit or loss	12,932	11,745
Accounts receivable	(354,340)	114,839
Accounts receivable - related parties	171,045	(177,212)
Other receivables	58,699	(22,171)
Other receivables - related parties	(134,110)	(6,666)
Inventories	1,903,269	(3,470,417)
Prepayments	(95,890)	(245,803)
Other current assets	128,215	455,125
Notes payable	24,176	-
Accounts payable	79,093	228,839
Accounts payable - related parties	107,469	45,400
Accrued expenses	59,496	(152,543)
Other payables	111,187	(64,825)
Other current liabilities	(1,447,347)	(1,234,575)
Accrued pension cost	(8,043)	(16,234)
Net cash used in operating activities	<u>(73,898)</u>	<u>(3,279,049)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from capital reduction of financial assets carried at cost	5,010	-
Proceeds from capital reduction of equity-method investments	-	6,621
Acquisition of properties	(1,572,569)	(1,538,165)
Proceeds from disposal of assets	1,081	-
Increase in refundable deposits	<u>(330)</u>	<u>(17,676)</u>
Net cash used in investing activities	<u>(1,566,808)</u>	<u>(1,549,220)</u>

(Continued)

# CHUNG HUNG STEEL CORPORATION

## STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2012 AND 2011 (In Thousands of New Taiwan Dollars)

	2012	2011
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Increase (decrease) in short-term loans	\$ (4,617,339)	\$ 3,099,906
Increase in commercial paper payable	119,495	1,419,313
Proceeds from long-term loans	11,472,800	1,980,000
Repayments of long-term loans	(5,364,286)	(857,143)
Increase in guarantee deposits received	-	35,000
Cash dividends	<u>-</u>	<u>(828,199)</u>
Net cash provided by financing activities	<u>1,610,670</u>	<u>4,848,877</u>
<b>NET INCREASE (DECREASE) IN CASH</b>	(30,036)	20,608
<b>CASH, BEGINNING OF YEAR</b>	<u>89,167</u>	<u>68,559</u>
<b>CASH, END OF YEAR</b>	<u>\$ 59,131</u>	<u>\$ 89,167</u>
<b>SUPPLEMENTAL CASH FLOW INFORMATION</b>		
Interest paid	\$ 254,900	\$ 156,347
Capitalized interest	<u>(12,188)</u>	<u>(5,290)</u>
Interest paid excluding capitalized interest	<u>\$ 242,712</u>	<u>\$ 151,057</u>
Income tax paid	<u>\$ -</u>	<u>\$ 8,230</u>
<b>INVESTING ACTIVITIES AFFECTING BOTH CASH AND NONCASH ITEMS</b>		
Acquisition of properties	\$ 1,490,644	\$ 1,489,887
Decrease in payable for properties purchased (including notes payable)	<u>81,925</u>	<u>48,278</u>
Cash paid	<u>\$ 1,572,569</u>	<u>\$ 1,538,165</u>
<b>NONCASH INVESTING AND FINANCING ACTIVITIES</b>		
Current portion of long-term loans	\$ 1,076,923	\$ -

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

(Concluded)

# CHUNG HUNG STEEL CORPORATION

## NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2012 AND 2011

(In Thousands of New Taiwan Dollars, Unless Stated Otherwise)

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### 1. ORGANIZATION AND OPERATIONS

Chung Hung Steel Corporation (the “Corporation”) was incorporated in September 1983 and started operations in September 1985. It mainly manufactures and sells steel products, such as cold and hot rolled coils and steel pipes. China Steel Corporation, the Corporation’s parent and major stockholder (41%), controls the Corporation’s management and operations.

The Corporation’s shares have been listed on the Taiwan Stock Exchange since February 1992.

As of December 31, 2012 and 2011, the Corporation had 931 and 919 employees, respectively.

### 2. SIGNIFICANT ACCOUNTING POLICIES

#### **Basis of Presentation**

The financial statements of the Corporation are prepared in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, Business Accounting Law, Guidelines Governing Business Accounting and accounting principles generally accepted in the Republic of China.

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

The Corporation’s significant accounting policies are summarized as follows:

#### **Foreign-currency Transactions**

Non-derivative foreign-currency transactions are recorded in New Taiwan dollars at the rates of exchange in effect when the transactions occur. Exchange differences arising from settlement of foreign-currency assets and liabilities are recognized in profit or loss.

At the balance sheet date, foreign-currency monetary assets and liabilities are revalued using prevailing exchange rates and the exchange differences are recognized in profit or loss.

#### **Accounting Estimates**

According to these guidelines, laws and principles, the Corporation is required to make certain assumptions and estimates, which affect the amounts of recorded assets, liabilities, revenues and expenses, including allowances for doubtful accounts and inventory losses, allowance for sales discounts, purchase contract loss, depreciation of properties, impairment loss on assets, pension cost, income tax, bonuses to employees, directors and supervisors, etc. Actual results could differ from these estimates.

## **Current and Noncurrent Assets and Liabilities**

Current assets include cash and those assets held primarily for trading purposes or to be realized, sold or consumed within one year from the balance sheet date. All other assets such as properties are classified as noncurrent. Current liabilities are obligations incurred for trading purposes or to be settled within one year from the balance sheet date. All other liabilities are classified as noncurrent.

## **Financial Instruments at Fair Value Through Profit or Loss**

Financial instruments at fair value through profit or loss include financial assets or financial liabilities held for trading. The Corporation recognizes a financial asset or a financial liability on its balance sheet when the Corporation becomes a party to the contractual provisions of the financial instrument. A financial asset is derecognized when the Corporation has lost 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. These financial instruments are initially recognized at fair value, and related transaction costs are expensed currently. When these instruments are remeasured at fair value, the changes in fair value are recognized under current income. A regular purchase or sale of financial assets is recorded using trade date accounting.

Derivatives that do not meet the criteria for hedge accounting are treated as financial assets or liabilities held for trading. When the fair value of the derivative is a positive number, the financial instrument is recorded as a financial asset; when the fair value is a negative number, the financial instrument is recorded 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. When these assets are subsequently measured at fair value, the changes in fair value are reported as a separate component of stockholders' equity. The accumulated gains or losses in stockholders' equity are recognized in earnings when the financial asset is derecognized from the balance sheet. A regular purchase or sale of financial assets is recorded using trade date accounting.

The recognition, derecognition and the fair value bases of available-for-sale financial assets are the same with those of financial assets at fair value through profit or loss.

Cash dividends received on investment in equity securities are recognized as income in the period received. Stock dividends received are recognized only as an increase in the number of shares of stock held on the ex-dividend date. Costs of investments sold are determined by the weighted-average method.

If there is objective evidence that a financial asset is impaired, an impairment loss is recognized. If 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.

The fair value of financial assets and financial liabilities at the balance sheet date are determined at the closing prices of publicly traded stocks.

## **Financial Assets Carried at Cost**

Investments in non-publicly traded stocks and stocks traded in the Emerging Stock Market are measured at their original cost. If there is objective evidence of financial asset impairment, impairment loss is recognized. No recording of a subsequent recovery of fair value is allowed.

## **Factoring of Accounts Receivable**

The following three conditions must be met to recognize factoring of accounts receivable:

- a. The accounts receivable have been legally isolated from the Corporation.
- b. The transferees have obtained the right to pledge or exchange the accounts receivable, which are either the transferred accounts receivable or the beneficial interest in the transferred assets.
- c. The transferor does not maintain effective control, through an agreement to repurchase or redeem the transferred accounts receivable before their maturity, over the transferred accounts receivable.

If the three conditions are met, the difference between the proceeds and the face value of the accounts receivable is recognized as a loss and recorded as nonoperating expense.

## **Impairment of Accounts Receivable**

As discussed in Note 3 to the financial statements, on January 1, 2011, the Corporation adopted the third-time revised Statement of Financial Accounting Standards (SFAS) No. 34, "Financial Instruments: Recognition and Measurement." One of the main revisions is that impairment of receivables originated by the Corporation should be covered by SFAS No. 34. Accounts receivable are assessed for impairment at the end of each reporting period and considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the accounts receivable, the estimated future cash flows of the asset have been affected. Objective evidence of impairment could include:

- Significant financial difficulty of the debtor;
- Accounts receivable becoming overdue;
- It becomes probable that the debtor will enter bankruptcy or financial re-organization.

Accounts receivable that are assessed as not impaired individually are further assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of accounts receivable could include the Corporation's past experience in the collection of payments, an increase in the number of delayed payments, as well as observable changes in national or local economic conditions that correlate with defaults on receivables.

The amount of the impairment loss recognized is the difference between the asset carrying amount and the present value of estimated future cash flows, after taking into account the related collateral and guarantees, discounted at the receivable's original effective interest rate. The carrying amount of the accounts receivable is reduced through the use of an allowance account.

## **Impairment of Asset**

If the recoverable amount of an asset (mainly properties, investments accounted for by the equity method and other assets) is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount.

If an impairment loss subsequently reverses, the carrying amount of the asset is increased accordingly, but the increased carrying amount may not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is recognized in earnings, unless the asset is carried at a revalued amount, in which case the reversal of the impairment loss is first recognized as gains to the extent that an impairment loss on the same revalued asset was previously charged to earnings. Any excess amount is treated as an increase in the unrealized revaluation increment.

For long-term equity investments in which the Corporation has significant influence but has no control, the carrying amount of each investment is compared with its own recoverable amount for the purpose of impairment testing.

### **Inventories**

Inventories consist of raw materials, supplies, work-in-process and finished goods. Inventories are stated at the lower of cost or net realizable value. Inventory write-downs are made by item, except where it may be appropriate to group similar or related items. Net realizable value is the estimated selling price of inventories less all estimated costs of completion and costs necessary to make the sale. Inventories are recorded at weighted-average cost on the balance sheet date.

### **Investments Accounted for by the Equity Method**

The equity method is applied to investments in companies in which the Corporation owns 20% or more of investees' common stock or exercises significant influence over their operating and financial policy decisions.

These investments are initially stated at cost, and their carrying amounts are subsequently adjusted for the Corporation's proportionate share in the net income or net loss and cumulative translation adjustment of the investee. Cash dividends received are accounted for as a reduction of the carrying value of the investments. When the investee recognizes net loss not recognized as pension cost and unrealized valuation gains or losses on financial instruments, the Corporation also records its equity in the investee's net loss not recognized as pension cost and unrealized gains or losses as an adjustment to stockholders' equity.

### **Properties**

Land is stated at cost or cost plus revaluation increment, and other properties are stated at cost less accumulated depreciation. Major additions, renewals and betterments are capitalized, while maintenance and repairs are expensed currently. Interest incurred during the construction and acquisition period is also capitalized as cost of the property.

Depreciation of the roller that belongs to the cold rolling department and the hot rolling department is calculated based on their level of wear. Others are calculated using the straight-line method over service lives estimated as follows: buildings and improvements, 10 to 60 years; machinery and equipment, 3 to 18 years; and other equipment, 3 to 18 years. Depreciation of the roller in the steel pipe department is calculated by the straight-line method over 5 years. Property still in use beyond their original estimated useful lives are further depreciated over their newly estimated useful lives.

Upon retirement or disposal of properties, the related cost (including revaluation increment), accumulated depreciation and the unrealized revaluation increment are removed from the accounts. Any gain or loss on disposal of the asset is included in nonoperating gains or losses in the year of disposal.

### **Rental Assets**

Rental assets are stated at the lower of carrying value (cost less accumulated depreciation) or recoverable value. Depreciation is calculated by the straight-line method over estimated service lives of 55 years.

### **Nonoperating Assets**

Nonoperating assets are stated at the lower of carrying value or net fair value.

## **Purchase Contract Losses**

Purchase contract losses pertain to losses on irrevocable raw materials purchase contracts. If the estimated costs of finished goods are in excess of their expected net realizable values, the excess is recorded as other liabilities, payable on purchase contract losses, and operating losses.

## **Deferred Credits**

Deferred credit is unrealized gain on the disposal of nonperforming loans and is recognized throughout the amortization period of the collaterals for these loans.

## **Pension**

Pension costs under the defined contribution plan are recognized on the basis of the Corporation's required monthly contributions to the employees' individual pension accounts.

Pension costs under the defined benefit plan are recognized on the basis of actuarial calculations. The balance of total pension obligation less the funded amounts is recorded as accrued pension cost. Payment of retirement benefits is made initially from the pension fund then charged against accrued pension costs, and any shortage will be charged to expense when paid.

## **Income Tax**

The Corporation applies the inter-year income tax allocation method. Tax effects of deductible temporary differences and unused loss carryforwards are recognized as deferred income tax assets. Valuation allowance is provided for deferred tax assets that are not certain to be realized. Tax effects of taxable temporary differences are recognized as deferred tax liabilities. 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 income 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.

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

According to the Income Tax Law, an additional tax at 10% of unappropriated earnings is provided for as income tax in the year the stockholders approve to retain the earnings.

## **Revenue Recognition**

Revenue is recognized when the titles to products and evident risks of ownership are transferred to customers, primarily upon shipment. Domestic sales are recognized when products are delivered to and accepted by the customers, and export sales are recognized when products are loaded onto shipping vessels in accordance with the sales terms.

Sales are measured at fair value, which is a price (net of trade discounts and sales discounts) agreed by the Corporation and customers. However, if the related receivables are due within one year, the differences between their fair values and receivable amounts are immaterial and sales transactions are frequent, the fair values of related receivables are not calculated using the discounted imputed interest rate.

Sales returns are recorded as reductions of sales in the year of actual return, and the related cost of sales is reversed to inventory. Sales allowances are monetary discounts given to customers when sales volume reaches a certain level and are recorded as sales allowances payable.

### 3. EFFECTS OF CHANGES IN ACCOUNTING PRINCIPLES

#### Financial Instruments

Starting January 1, 2011, the Corporation adopted the newly revised Statement of Financial Accounting Standards (SFAS) No. 34, "Financial Instruments: Recognition and Measurement." The main revisions include: (1) finance lease receivables impairment are now covered by SFAS No. 34; (2) the scope of the applicability of SFAS No. 34 to insurance contracts is amended; (3) loans and receivables originated by the enterprise are now covered by SFAS No. 34; (4) additional guidelines on impairment of financial assets carried at amortized cost when the debtor has financial difficulties and the terms of obligations have been modified; and (5) accounting treatment by a debtor for modifications in the terms of obligations. This accounting change did not have a significant impact on the financial statements as of and for the year ended December 31, 2011.

#### Operating Segments

Starting January 1, 2011, the Corporation adopted the newly issued SFAS No. 41, "Operating Segments." The requirements of the statement are based on the information about the components of the Corporation that management uses to make decisions about operating matters. SFAS No. 41 requires identification of operating segments on the basis of internal reports that are regularly reviewed by the Corporation's chief operating decision maker in order to allocate resources to the segments and assess their performance. This statement supersedes SFAS No. 20, "Segment Reporting." The information for the year ended December 31, 2010 has been recast to conform to SFAS No. 41. Disclosure of segment information is made in the consolidated financial statements.

### 4. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

The Corporation entered into derivative contracts during the years ended December 31, 2012 and 2011 to manage exposures due to exchange rate and interest rate fluctuations. The financial risk management objective of the Corporation is to minimize risks due to changes in fair value or cash flows. Derivatives that do not meet the criteria for hedge accounting are treated as financial assets or liabilities held for trading.

Outstanding forward exchange contracts as of December 31, 2012 and 2011 were as follows:

	Currency	Maturity Date	Amount (In Thousands)
<u>December 31, 2012</u>			
Buy	NTD/JPY	2013.02.27-2014.12.30	NT\$33,145/JPY92,540
Buy	NTD/USD	2013.01.02-2014.04.30	NT\$945,876/USD32,500
Buy	NTD/EUR	2013.11.12	NT\$70,247/EUR1,906
<u>December 31, 2011</u>			
Buy	NTD/JPY	2012.10.30-2014.12.30	NT\$296,821/JPY832,860

	<u>Year Ended December 31</u>	
	<b>2012</b>	<b>2011</b>
Financial assets at fair value through profit or loss	\$ 3,423	\$ 28,565
Less: Noncurrent portion	<u>259</u>	<u>23,979</u>
	<u>\$ 3,164</u>	<u>\$ 4,586</u>
Financial liabilities at fair value through profit or loss	\$ 5,476	\$ -
Less: Noncurrent portion	<u>1,739</u>	<u>-</u>
	<u>\$ 3,737</u>	<u>\$ -</u>

Net loss and net gain on financial assets at fair value through profit or loss for the years ended December 31, 2012 and 2011 were NT\$11,585 thousand and NT\$29,111 thousand, respectively; net losses on financial liabilities at fair value through profit or loss for the years ended December 31, 2012 and 2011 were NT\$6,101 thousand and NT\$827 thousand, respectively.

## 5. ACCOUNTS RECEIVABLE

As of December 31, 2012 and 2011, there were no allowances for doubtful accounts.

The Corporation entered into accounts receivable factoring contract (without recourse) with Mega International Commercial Bank ("Mega Bank"). Under the contract, the Corporation is authorized to sell accounts receivable to Mega Bank upon the delivery of products to customers and is required to complete related formalities on the next banking day. Under this contract, the Corporation does not bear the risk of the uncollectibility of the accounts receivable. The receivables sold and the related credit lines, which may be used on a revolving basis, were as follows:

Buyer of Accounts Receivable	Advances Received at Beginning of Year	Receivables Sold	Amounts Collected	Advances Received at Year-end	Interest Rates on Advances Received (%)	Credit Line
Year ended <u>December 31, 2012</u>						
Mega Bank	<u>\$ 1,221,416</u>	<u>\$ 3,753,783</u>	<u>\$ 3,571,357</u>	<u>\$ 1,403,842</u>	1.40	\$3 billion
Year ended <u>December 31, 2011</u>						
Mega Bank	<u>\$ 922,320</u>	<u>\$ 3,252,218</u>	<u>\$ 2,953,122</u>	<u>\$ 1,221,416</u>	1.30	\$3 billion

## 6. INVENTORIES

	<u>December 31</u>	
	<b>2012</b>	<b>2011</b>
Raw materials	\$ 2,765,913	\$ 4,952,849
Supplies	420,115	396,459
Work-in-process	752,941	735,795
Finished goods	2,090,474	2,374,670
		(Continued)

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Others	\$ 10,208	\$ 7,817
Raw materials and supplies in transit	<u>592,209</u>	<u>325,605</u>
	<u>\$ 6,631,860</u>	<u>\$ 8,793,195</u>

(Concluded)

As of December 31, 2012 and 2011, the allowance for inventory devaluation was NT\$258,066 thousand and NT\$1,109,130 thousand, respectively, and was recorded as reduction in inventories.

The cost of inventories recognized as cost of goods sold in the years ended December 31, 2012 and 2011 was NT\$44,374,682 thousand and NT\$47,638,858 thousand, respectively. The items recognized as cost of goods sold were as follows:

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Allowance for loss on inventories (including loss from borrowed materials)	\$ 259,945	\$ 1,129,124
Deduction of the allowance for inventory devaluation	(1,109,130)	(450,020)
Deduction of the allowance for borrowed materials devaluation	(19,994)	(49,351)
Allowance for purchase contract loss	846,325	1,579,220
Income from supplies and scraps	(1,004,809)	(1,175,726)

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

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Domestic quoted stocks		
China Steel Corporation	\$ 840,116	\$ 840,116
Adjustments for appraisal (Note 18)	<u>321,637</u>	<u>365,150</u>
	<u>\$ 1,161,753</u>	<u>\$ 1,205,266</u>

#### 8. FINANCIAL ASSETS CARRIED AT COST - NONCURRENT

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Emerging market stocks		
Yieh United Steel Corp.	\$ 257,600	\$ 257,600
Domestic unquoted common stocks		
RiselinK Venture Capital Corp.	24,990	30,000
Pacific Harbour Stevedoring Corp.	2,750	2,750
Cheng Shin House Management Consulting Corp.	<u>285</u>	<u>285</u>
	<u>\$ 285,625</u>	<u>\$ 290,635</u>

Riselink Venture Capital Corp. conducted capital reduction and refunded NT\$5,010 thousand to the Corporation in July 2012.

The Corporation also had investments in Grand Fortune Special Steel Co. Ltd., Chateau Bridge Top Inc., Taiwan Vespa and Sol Hwang Enterprise. The carrying amounts of these investments were reduced to zero because of impairment losses on these investments.

Stocks which have no quoted prices in active market and of which verifiable fair values cannot be determined at a reasonable cost, are carried at cost.

## 9. INVESTMENTS ACCOUNTED FOR BY THE EQUITY METHOD

	<b>December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% of Owner- ship</b>	<b>Amount</b>	<b>% of Owner- ship</b>
Hung Li Steel Corp. (HLC)	\$ 2,635,353	100	\$ 2,828,024	100
Transglory Investment Corp. (TIC)	2,304,196	41	2,318,687	41
Hong Kao Investment Corp. (HKIC)	30,959	100	37,026	100
Taiwan Steel Corp. (TSC)	<u>26,337</u>	100	<u>26,152</u>	100
	<u>\$ 4,996,845</u>		<u>\$ 5,209,889</u>	

Significant movements were as follows:

TSC reduced capital to offset deficit of NT\$23,745 thousand and to return cash of NT\$6,621 thousand in June 2011, which resulted in the decrease in common stock by 3,037 thousand shares.

The recognition of the following investment income (loss) from investments accounted for by the equity method was based on the investees' audited financial statements for the same reporting periods as those of the Corporation:

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
HLC	\$ (192,671)	\$ (89,155)
TIC	92,093	207,887
TSC	185	152
HKIC	<u>131</u>	<u>3,023</u>
	<u>\$ (100,262)</u>	<u>\$ 121,907</u>

The Corporation's consolidated financial statements included HLC, HKIC and TSC.

## 10. PROPERTIES

Accumulated depreciation consisted of:

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Buildings and improvements	\$ 1,016,300	\$ 957,995
Machinery and equipment	10,884,258	9,807,280
Spare parts	506,376	466,185
Other equipment	<u>2,428,768</u>	<u>2,189,014</u>
	<u>\$ 14,835,702</u>	<u>\$ 13,420,474</u>

Interest expenses capitalized were as follows:

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
Total interest expenses	\$ 264,942	\$ 163,671
Capitalized interest	<u>(12,188)</u>	<u>(5,290)</u>
Interest expenses reflected in the income statement	<u>\$ 252,754</u>	<u>\$ 158,381</u>
Capitalization rate	1.16%-1.37%	0.96%-1.15%

The Corporation revalued its land in September 2011, which resulted in total revaluation increments of NT\$331,820 thousand. The net revaluation amount of NT\$187,386 thousand after deducting the reserve for land value increment tax of NT\$144,434 thousand was credited to equity as unrealized revaluation increment.

## 11. OTHER ASSETS

### a. Rental assets

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Land - Kaohsiung Long Dong Section	\$ 2,640,958	\$ 2,640,958
Land - Taipei office	64,026	64,026
Buildings and improvements - Taipei office	<u>30,289</u>	<u>30,289</u>
	2,735,273	2,735,273
Less: Accumulated depreciation	<u>8,893</u>	<u>8,349</u>
	<u>\$ 2,726,380</u>	<u>\$ 2,726,924</u>

On June 30, 2010, the Corporation entered into a contract with a third party on the lease of the Corporation's land in Kaohsiung Long Dong Section.

Based on the lease contract, the rental is collectible monthly, and the rental is subject to change intermittently from the construction period throughout the building operating period.

On the lessee's obtaining of a building license on December 16, 2010, the Corporation started to collect the construction period rental of NT\$2,941 thousand per month and the operating period rental of NT\$5,883 thousand per month. The lessee began to operate in August 2011. The rental revenue for the years ended December 31, 2012 and 2011 were NT\$71,048 thousand and NT\$47,794 thousand, respectively, and were included in nonoperating income and gains. Based on the lease contract, in August 2011, the Corporation obtained the deposit of NT\$35,000 thousand which was recognized as guaranteed deposits received.

As of December 31 2012, the total amount of future rentals payables and their present value were as follows:

Year	Future Rentals Payables	Present Value of Future Rentals Payables
2013	\$ 70,591	\$ 70,591
2014	71,768	71,768
2015	74,121	74,121
2016-2020	389,260	361,338
2021-2025	432,680	375,400
2026-2030	477,704	387,329
January - August 2031	<u>67,120</u>	<u>52,393</u>
	<u>\$ 1,583,244</u>	<u>\$ 1,392,940</u>

The present value of the above future rentals payables over five years was discounted at the interest rate (1.355%) quoted by the Bank of Taiwan for a one-year time deposit.

As of December 31, 2012 and 2011, notes received and advance rental were as follows:

	<u>December 31</u>	
	2012	2011
Notes receivable received	\$ 43,237	\$ 43,237
Less: Advance rental	<u>(43,237)</u>	<u>(43,237)</u>
	<u>\$ -</u>	<u>\$ -</u>

The Corporation leased the Taipei office to third party under a renewable operating lease contract. The rental revenue was NT\$285 thousand per month from January to June in 2012 and NT\$304 thousand per month from July, 2012.

On the basis of the related land appraisal reports, the Corporation recognized a gain on the impairment loss reversal amounting to NT\$182,127 thousand (NT\$143,627 thousand for Long Dong Section and NT\$38,500 thousand for Taipei office). The gain was included in nonoperating income and gains.

b. Nonoperating assets, net

	<u>December 31</u>	
	2012	2011
Land		
Kaohsiung Long Hua Section	\$ 226,557	\$ 226,557
Tainan Kuo An Section	2,782,496	2,782,496
Luzhu Hou Xiang Section	<u>122,502</u>	<u>122,502</u>
	<u>3,131,555</u>	<u>3,131,555</u>

(Continued)

	<u>December 31</u>	
	<b>2012</b>	<b>2011</b>
Less		
Accumulated impairment loss - Kaohsiung Long Hua Section	\$ 52,692	\$ 52,692
Accumulated impairment loss - Tainan Kuo An Section	<u>1,636,921</u>	<u>1,636,921</u>
	<u>1,689,613</u>	<u>1,689,613</u>
	<u>\$ 1,441,942</u>	<u>\$ 1,441,942</u>

On the basis of the related land appraisal reports, the Corporation recognized a gain on the impairment loss reversal amounting to NT\$164,844 thousand (NT\$50,152 thousand for Long Hua Section, NT\$87,942 thousand for Kuo An Section and NT\$26,750 thousand for Luzhu Hou Xiang Section). The gain was included in nonoperating income and gains in 2011.

c. Others

The Corporation bought farmlands for warehousing at the Jia Xing Section and Bai Mi Section of the Gangshan Town in Kaohsiung City. However, certain regulations prohibit the Corporation from registering the title of these farmlands in the Corporation's name; thus, the registration was made in the name of an individual person. The individual person consented to fully cooperate with the Corporation in changing the land title in the future and pledged the land to the Corporation as collateral.

The Kaohsiung City Government levied some parts of Jia Xing Section farmlands in May 2012. As of December 31, 2012 and 2011, the book value of those levied farmlands was NT\$66,753 thousand and NT\$66,823 thousand, respectively.

## 12. SHORT-TERM LOANS

	<u>December 31</u>	
	<b>2012</b>	<b>2011</b>
Revolving loans - interest of 1.05%-1.21% in 2012 and 0.95%-1.15% in 2011	\$ 5,283,000	\$ 7,919,680
Letter of credit loans - interest of 0.55%-1.23% in 2012 and 0.95%-1.15% in 2011	2,682,530	4,660,986
Bank overdraft - interest of 0.63% in 2012 and 0.619% in 2011	<u>253,691</u>	<u>255,894</u>
	<u>\$ 8,219,221</u>	<u>\$ 12,836,560</u>

## 13. COMMERCIAL PAPER PAYABLE

	<u>December 31</u>	
	<b>2012</b>	<b>2011</b>
Commercial paper - interest of 0.785%-0.912% in 2012 and 0.762%-0.89% in 2011	\$ 1,670,000	\$ 1,550,000
Less: Unamortized discounts	<u>1,205</u>	<u>700</u>
	<u>\$ 1,688,795</u>	<u>\$ 1,549,300</u>

## 14. LONG-TERM LOANS

	<u>December 31</u>	
	<u>2012</u>	<u>2011</u>
Syndicated bank loans		
Taiwan Bank		
Type A	\$ 6,980,000	\$ -
Type B	4,500,000	-
Mega International Commercial Bank, etc.		
Type A	-	1,714,286
Revolving credit loan		
Mega Bank	-	825,000
TCB Bank	-	825,000
Land Bank	-	550,000
Taiwan Business Bank	-	550,000
Taipei Fubon Bank	-	550,000
Taishin Bank	-	<u>330,000</u>
	<u>11,480,000</u>	<u>5,344,286</u>
Less: Current portion	1,076,923	-
Syndicated loan fee	<u>23,962</u>	<u>5,950</u>
	<u>\$ 10,379,115</u>	<u>\$ 5,338,336</u>

In September 2006, the Corporation entered into a syndicated credit facility agreement with Mega International Commercial Bank (“Mega Bank”) and 20 other banks, as follows:

- a. The credit line is NT\$14 billion, which consists of Type A NT\$6 billion, Type B NT\$5 billion and Type C NT\$3 billion. The first drawdown of the Corporation was on October 23, 1996. The Corporation canceled Type C in October, 2010 and cancelled Type B in February, 2011.
- b. Type A is a secured loan (non-revolving credit). The loan balance is repayable in 14 installments from April 2007 to October 2013; however, the loan was repaid in advance in March 2012. As of December 31, 2011, the interest rate was 1.4535%.

In December 2010, the Corporation entered into a medium-term loan agreement with Mega International Commercial Bank and 5 other banks, as follows:

- a. The credit line is NT\$6.6 billion; the first drawdown of the Corporation was on December 30, 2010.
- b. The debt instrument is an unsecured revolving credit loan, and the minimum rate of the commitment to use is 25% of the loan amount and the loan term is 90 days. When the committed minimum amount to use is exceeded, the selection of a 60-, 90- or 180- day loan term must be made before every use. On making an application for loan use, the principal plus interest should be paid in full by the due date. The debt was repaid in advance in March 2012 and the interest rate was 1.5155% at the end of year 2011.

In December 2011, the Corporation entered into a syndicated credit facility agreement with Taiwan Bank and 11 other banks, as follows:

- a. The credit line is NT\$16 billion, which consists of Type A NT\$7 billion and Type B NT\$9 billion. The first drawdown of the Corporation was on March 20, 2012.

- b. Type A is a secured loan (non-revolving credit). The loan balance is repayable in 13 installments from March 2013 to March 2019. As of December 31, 2012, the interest rate was 1.5856%.
- c. Type B is an unsecured revolving credit loan, and the minimum rate of commitment to use is 25% of the loan amount. The selection of a 30-, 60-, 90- or 180-day loan term must be made before every use. On making an application for loan use, the principal plus interest should be paid in full by the due date. Furthermore, the Corporation can notify the bank of the renewal of the loan with the same conditions three business days before the due date. And for the same amount as a previous borrowing, the completed remittance procedures do not have to be required to complete the repeated again. As of December 31, 2012, the interest rate was between 1.6047% and 1.6110%.
- d. Under the agreement, China Steel Corporation and its related parties should collectively hold at least 30% of the Corporation's issued shares and control the Corporation's operation. From January 1, 2012, the net tangible assets of the Corporation should not be less than half of the capital, and the ratio of financial liabilities to net tangible assets should not exceed 350%.

The amounts referred to the above restrictions should be based on audited annual financial statements. If the Corporation breaches the agreement, the Corporation should take remedial measures within six months from the next day after the issue date of the financial statements' or adjust the interest rate and the rate of the guarantee fee in accordance with the agreement.

- e. As of December 31, 2012, the Corporation was in compliance with this syndicated credit facility agreement.

## 15. ACCRUED EXPENSES

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Salary and bonus	\$ 99,794	\$ 108,946
Utilities	70,581	55,565
Export fee	70,301	42,463
Outsourced construction	64,458	-
Delivery pay	38,760	38,305
Processing charge (Note 23)	33,118	43,755
Others	<u>70,815</u>	<u>99,297</u>
	<u>\$ 447,827</u>	<u>\$ 388,331</u>

## 16. OTHER PAYABLES

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Sales discount (Note 2)	\$ 228,246	\$ 121,801
Sale on consignment (Note 23)	76,375	63,342
Properties purchased	39,232	124,157
Others	<u>3,690</u>	<u>11,981</u>
	<u>\$ 347,543</u>	<u>\$ 321,281</u>

## 17. PENSION PLAN

The pension plan under the Labor Pension Act (LPA) is a defined contribution plan. Based on the LPA, the rate of the Corporation's monthly contributions to employees' individual pension accounts is at 6% of monthly salaries and wages. Related pension costs were NT\$11,378 thousand for 2012 and NT\$10,494 thousand for 2011.

The Corporation has a retirement plan in accordance with the Labor Standards Law. Retirement benefits are based on employee's length of service and his/her average salaries and wages of the last six months before retirement.

The Corporation contributes amounts equal to 12.9% of total monthly salaries and wages to a pension fund administered by the pension fund monitoring committee. The pension fund is deposited in the Bank of Taiwan in the committee's name.

Other information on the defined benefit plan is as follows:

a. Components of net pension cost

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
Service cost	\$ 22,605	\$ 26,526
Interest cost	17,921	16,884
Projected return on plan assets	(14,861)	(13,565)
Amortization	<u>11,435</u>	<u>11,435</u>
Net pension cost	<u>\$ 37,100</u>	<u>\$ 41,280</u>

b. Reconciliation of the fund status of the plan and accrued pension cost

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Benefit obligations		
Vested	\$ 536,327	\$ 545,652
Non-vested	<u>199,089</u>	<u>190,408</u>
Accumulated	735,416	736,060
Additional benefits based on future salaries	<u>177,445</u>	<u>160,029</u>
Projected benefit obligations	912,861	896,089
Fair value of plan assets	<u>(736,520)</u>	<u>(716,319)</u>
Fund status	176,341	179,770
Unrecognized prior service cost	(42,058)	(47,315)
Unrecognized net transition obligation	(6,177)	(12,355)
Unrecognized net actuarial gain (loss)	<u>(2,122)</u>	<u>13,927</u>
Accrued pension cost	<u>\$ 125,984</u>	<u>\$ 134,027</u>
Vested benefits	<u>\$ 752,753</u>	<u>\$ 761,863</u>

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
c. Actuarial assumptions		
Discount rate used in determining present value	1.875%	2.000%
Future salary increase rate	2.000%	2.000%
Expected rate of return on plan assets	1.875%	2.000%
d. Contributions to the fund during the year	<u>\$ 45,143</u>	<u>\$ 57,514</u>
e. Payments from the fund during the year	<u>\$ 31,968</u>	<u>\$ 4,616</u>

## 18. STOCKHOLDERS' EQUITY

### a. Common stock

In June 2009, the Corporation revised the number of its authorized shares to 3,000,000 shares upon obtaining the approval in the stockholders' meeting. However, because the Company Law prohibits the Corporation from revising the number of authorized shares before the full issuance of the original authorized shares, the number of authorized shares remained unchanged.

In June 2011, the stockholders approved a capital increase through issuance of stock dividends in the amount of NT\$552,132 thousand. The Corporation had completed the registration requirements for this capital increase. As of December 31, 2012, the Corporation's issued and outstanding shares amounted to NT\$14,355,444 thousand.

The Corporation issued shares at a discount; related information was as follows:

<b>Date</b>	<b>Number of Shares Issued (In Thousand)</b>	<b>Par Value</b>
March 31, 2009	400,000	\$9.5

### b. Capital surplus

Under the Company Law, capital surplus can only be used to offset a deficit. However, the capital surplus from shares issued in excess of par (additional paid-in capital from issuance of common shares, conversion of bonds and treasury stock transactions) and donations may be capitalized, which however is limited to a certain percentage of the Corporation's paid-in capital. Under the revised Company Law promulgated on January 4, 2012, the aforementioned capital surplus also may be distributed in cash when the Corporation incurs no loss. The capital surplus from long-term investments accounted for under the equity method may not be used for any purpose.

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
Long-term investments	\$ 342,007	\$ 342,052
Additional paid in capital	<u>903</u>	<u>903</u>
	<u>\$ 342,910</u>	<u>\$ 342,955</u>

In October, 2008, TGIC exchanged its common stock and preferred stock of Dragon Steel Corporation for China Steel Corporation's ("CSC") common stock. The Corporation recognized the disposal gain on long-term investment at its percentage of ownership in TIC.

In 2009, CSC had transferred its treasury stocks to its employees and subsidiaries. The Corporation recognized a salary expense of NT\$743 thousand.

In July 2011, CSC issued common shares for cash capital. Under the Company Law, CSC should reserve 10% of the stock options for its employees and subsidiaries. The Corporation recognized NT\$160 thousand of compensation cost.

c. Appropriation of retained earnings and dividend policy

Before June, 2012, the Corporation's Articles of Incorporation provide that from annual net income less any prior years' deficit, 10% should be set aside as legal reserve and a certain percentage as special reserve based on relevant laws or regulations or as requested by the authorities in charge. The remaining earnings should be appropriated in accordance with the resolution passed at a stockholders' meeting if the dividend per share is not lower than NT\$0.02. The appropriation should include (a) at least 0.3% as bonus to employees and (b) 1% as remuneration to directors and supervisors.

The Corporation is in a mature steel industry. Thus, dividends will be appropriated in cash or in stock at an appropriate ratio, with cash dividends to be at least 50% of total dividends.

The Corporation's revised Articles of Incorporation, proposed and approved in the shareholders' meeting in June, 2012, provide that the annual net income, less any deficit, should be appropriated in the following order:

- 1) 10% as legal reserve;
- 2) A certain percentage as special reserve;
- 3) Of the remainder, 1% as remuneration to directors and supervisors and at least 0.3% as bonus to employees;
- 4) The remainder may be declared as dividends or retained as proposed and approved in the shareholders' meetings.

The Corporation is in a mature steel industry. Thus, dividends will be appropriated in cash or in stock at an appropriate ratio, with cash dividends to be at least 50% of total dividends.

The Corporation had accumulated deficits in both 2012 and 2011; thus, the Corporation did not estimate any bonuses to employees and remuneration to directors and supervisors. If the actual amounts subsequently resolved by the stockholders differ from the proposed amounts, the differences are recorded in the year of stockholders' resolution as a change in accounting estimate. If a share bonus is resolved to be distributed to employees, the number of shares is determined by dividing the amount of the share bonus by the closing price (after considering the effect of cash and stock dividends) of the shares of the day immediately preceding the stockholders' meeting.

Based on a directive issued by the Securities and Futures Bureau, an amount equal to the net debit balance of certain stockholders' equity accounts (including unrealized gain or loss on financial instruments and net loss not recognized as pension cost) shall be transferred from unappropriated earnings to a special reserve. Any special reserve appropriated may be reversed to the extent of the decrease in the net debit balance.

Under the Company Law, legal reserve should be appropriated from retained earnings until its balance equals the Corporation's paid-in capital. Legal reserve may be used to offset a deficit. Under the revised Company Law issued on January 4, 2012, when the Corporation incurs no loss and the legal reserve has exceeded 25% of the Corporation's paid-in capital, the excess may be transferred to capital or distributed in cash.

The appropriation of 2010 earnings proposed by the board of directors in March 2011 and approved in the stockholders' meeting in June 2011 was as follows:

	<u>For Year 2010</u>	
	<b>Appropriation of Earnings</b>	<b>Dividends Per Share (NT\$)</b>
Legal reserve	\$ 154,487	\$ 0.6
Cash dividends	828,199	0.4
Stock dividends	<u>552,132</u>	
	<u>\$ 1,534,818</u>	

The use of legal reserve to offset the 2011 deficit was proposed by the board of directors in March 2012 and approved in the stockholders' meeting in June 2012.

The bonus to employees and remuneration to directors and supervisors for 2010 approved in the stockholders' meeting in June 2011 and the accrual amounts reflected in the financial statements for the year ended December 31, 2010 were as follows:

	<u>Year Ended December 31, 2010</u>	
	<b>Bonus to Employee</b>	<b>Remuneration to Directors and Supervisors</b>
Amounts approved in shareholders' meetings	\$ 73,422	\$ 14,684
Amounts recognized respective financial statements	<u>(111,236)</u>	<u>(13,904)</u>
	<u>\$ (37,814)</u>	<u>\$ 780</u>

The differences between the approved amounts of the bonus to employees and the remuneration to directors and supervisors and the accrual amounts reflected in financial statements for the year ended December 31, 2010 which were primarily due to changes in estimates had been adjusted in profit and loss for the year ended December 31, 2011.

Information on earnings appropriation, bonus to employees, directors and supervisors, and offsetting of deficit is available on the Market Observation Post System on the Web site of the Taiwan Stock Exchange Corporation.

d. Unrealized revaluation increment

Unrealized revaluation increment was as follows:

	<u>December 31</u>	
	<b>2012</b>	<b>2011</b>
The Corporation (Note 10)	\$ 187,386	\$ 187,386
Equity-method investments	<u>169,511</u>	<u>169,511</u>
	<u>\$ 356,897</u>	<u>\$ 356,897</u>

e. Unrealized gain or loss on financial instruments

In 2012 and 2011, movements of unrealized gain (loss) on financial instruments were as follows:

	<b>Available-for- sale Financial Assets</b>	<b>Equity-method Investments</b>	<b>Total</b>
<u>Year ended December 31, 2012</u>			
Balance, beginning of year	\$ 365,150	\$ (609,963)	\$ (244,813)
Recognized in stockholders' equity	<u>(43,513)</u>	<u>(107,537)</u>	<u>(151,050)</u>
Balance, end of year	<u>\$ 321,637</u>	<u>\$ (717,500)</u>	<u>\$ (395,863)</u>
<u>Year ended December 31, 2011</u>			
Balance, beginning of year	\$ 495,083	\$ (287,920)	\$ 207,163
Recognized in stockholders' equity	<u>(129,933)</u>	<u>(322,043)</u>	<u>(451,976)</u>
Balance, end of year	<u>\$ 365,150</u>	<u>\$ (609,963)</u>	<u>\$ (244,813)</u>

## 19. INCOME TAX

- a. A reconciliation of income tax expense based on income before income tax at the 17% statutory rate and income tax expense (benefit) was as follows:

	<u>Years Ended December 31</u>	
	<b>2012</b>	<b>2011</b>
Benefit on pretax loss at the statutory rate	\$ (590,456)	\$ (414,747)
Tax effect of adjusting items:		
Permanent differences		
Investment loss (income) under the equity method	17,045	(20,724)
Dividend income	(7,330)	(18,470)
Reversal of impairment loss	-	(58,985)
Others	5,343	(2,372)
Temporary differences		
Unrealized (realized) discounts on sales	16,318	(16,721)
Unrealized (realized) loss on purchase contract	(97,716)	55,825
Unrealized (realized) loss on inventories	(147,760)	107,058
Realized deferred gain on disposal of nonperforming loans	(13,964)	(13,965)
Pension difference	(1,368)	(2,759)
Others	<u>7,892</u>	<u>(2,510)</u>
Income tax benefit before tax credits	(811,996)	(388,370)
Allowance for loss carryforwards	<u>811,996</u>	<u>388,370</u>
Current income tax expense	<u>-</u>	<u>-</u>
Deferred income tax expense		
Temporary differences	236,598	(126,928)
Loss carryforwards	(777,000)	(387,898)
Adjustment to valuation allowance	<u>540,402</u>	<u>514,826</u>
	<u>-</u>	<u>-</u>
Adjustments to prior years' tax	<u>(60)</u>	<u>8,230</u>
Income tax expense (benefit)	<u>\$ (60)</u>	<u>\$ 8,230</u>

b. Deferred income tax assets (liabilities) were as follows:

	<u>December 31</u>	
	<u>2012</u>	<u>2011</u>
<b>Current</b>		
Deferred income tax assets		
Sales discount payable	\$ 37,024	\$ 20,706
Purchase contract loss	-	97,716
Allowance for inventory loss	44,191	191,951
Others	<u>8,986</u>	<u>6,265</u>
	90,201	316,638
Less: Valuation allowance	<u>89,272</u>	<u>310,538</u>
	<u>929</u>	<u>6,100</u>
<b>Deferred income tax liabilities</b>		
Unrealized valuation gains on financial instruments	-	(4,856)
Others	<u>(929)</u>	<u>(1,244)</u>
	<u>(929)</u>	<u>(6,100)</u>
	<u>-</u>	<u>-</u>
<b>Noncurrent</b>		
Deferred income tax assets		
Loss carryforwards	1,399,981	622,981
Gain on disposal of nonperforming loans	167,739	181,703
Unfunded pension cost	<u>21,417</u>	<u>22,785</u>
	1,589,137	827,469
Less: Valuation allowance	<u>1,589,137</u>	<u>827,469</u>
	<u>-</u>	<u>-</u>
Total deferred income tax assets	<u>\$ -</u>	<u>\$ -</u>

Valuation allowance is fully provided for deferred tax assets because the steel industry constantly changes.

Loss carryforwards as of December 31, 2012 comprised of:

<u>Unused Amount</u>	<u>Expiry Year</u>
\$ 1,380,064	2019
2,078,673	2021
<u>4,776,448</u>	2022
<u>\$ 8,235,185</u>	

c. The tax returns through 2010 had been examined and cleared by the tax authorities.

d. Information on integrated income tax is as follows:

For distribution of earnings generated on or after January 1, 1998, the ratio for the imputation credits allocated to stockholders of the Corporation is based on the balance of the imputation credit account (ICA) as of the date of dividend distribution. As of December 31, 2012 and 2011, the balances of the imputation credits which can be allocated to the stockholders amounted to NT\$908,782 thousand and NT\$898,438 thousand, respectively.

The creditable ratio for the distribution of the 2010 earnings was 20.48%.

## 20. PERSONNEL, DEPRECIATION AND AMORTIZATION

	Years Ended December 31							
	2012				2011			
	Operating Costs	Operating Expenses	Others	Total	Operating Costs	Operating Expenses	Others	Total
Personnel								
Salary (including annual bonus)	\$ 470,742	\$ 113,752	\$ -	\$ 584,494	\$ 503,323	\$ 104,286	\$ -	\$ 607,609
Insurance	47,221	9,306	-	56,527	46,320	8,594	-	54,914
Pension cost	39,922	8,556	-	48,478	43,870	7,904	-	51,774
Welfare benefits	167,323	30,188	-	197,511	192,509	32,070	-	224,579
Other	3,471	3,260	-	6,731	3,057	3,160	-	6,217
	<u>\$ 728,679</u>	<u>\$ 165,062</u>	<u>\$ -</u>	<u>\$ 893,741</u>	<u>\$ 789,079</u>	<u>\$ 156,014</u>	<u>\$ -</u>	<u>\$ 945,093</u>
Depreciation	\$ 1,599,608	\$ 4,507	\$ 544	\$ 1,604,659	\$ 1,554,077	\$ 4,433	\$ 543	\$ 1,559,053
Amortization	-	-	-	-	-	7,030	-	7,030

Depreciation referred to properties and rental assets; depreciation of rental assets was recognized as a reduction of rental revenue.

## 21. BASIC LOSS PER SHARE

The numerators and denominators used in the computation of EPS were as follows:

### a. Numerator, net loss

	Years Ended December 31			
	2012		2011	
	Before Tax	After Tax	Before Tax	After Tax
Net loss	<u>\$ (3,473,271)</u>	<u>\$ (3,473,211)</u>	<u>\$ (2,439,686)</u>	<u>\$ (2,447,916)</u>

### b. Denominator - shares (thousands)

	Years Ended December 31	
	2012	2011
Weighted average of outstanding common shares	1,435,544	1,380,331
Add: Capitalization of retained earnings	-	55,213
	<u>1,435,544</u>	<u>1,435,544</u>

## 22. FINANCIAL INSTRUMENTS

### a. As of December 31, 2012 and 2011, the fair values of financial instruments were as follows:

	December 31			
	2012		2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<u>Nonderivative financial instruments</u>				
Assets				
Available-for-sale financial assets - noncurrent	\$ 1,161,753	\$ 1,161,753	\$ 1,205,266	\$ 1,205,266
Financial assets carried at cost - noncurrent	285,625	-	290,635	-
Refundable deposits	22,224	22,224	21,894	21,894

(Continued)

	<b>December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Carrying Value</b>	<b>Fair Value</b>	<b>Carrying Value</b>	<b>Fair Value</b>
Liabilities				
Long-term loans (including current portion)	\$11,456,038	\$11,456,038	\$ 5,338,336	\$ 5,338,336
Guarantee deposits received	35,000	35,000	35,000	35,000
<u>Derivative financial instruments</u>				
Forward contracts				
Financial assets at fair value through profit and loss - current	3,164	3,164	4,586	4,586
Financial assets at fair value through profit and loss - noncurrent	259	259	23,979	23,979
Financial liabilities at fair value through profit and loss - current	3,737	3,737	-	-
Financial liabilities at fair value through profit and loss - noncurrent	1,739	1,739	-	-
				(Concluded)

b. The assumptions and methods used to estimate the fair values of financial instruments are as follows:

- 1) The carrying values of cash, notes and accounts receivable, accounts receivable from related parties, other receivables, other receivables from related parties, restricted assets - current, short-term loans, commercial paper payable, notes and accounts payable, accounts payable to related parties, accrued expenses and other payables, approximate fair value because of the short maturities of these instruments.
- 2) The fair values of available-for-sale financial assets are determined at their market value.

If derivative financial instruments have no market values, the fair values are determined using valuation methods incorporating assumptions consistent with those used in the market. The fair values of forward contracts are calculated at exchange rates quoted by financial institutions on the maturity dates.

- 3) Financial assets carried at cost are investments in unquoted shares and stocks traded in the Emerging Stock Market, which have no quoted prices in an active market and entail an unreasonably high cost to obtain verifiable fair value. Therefore, no fair value is presented.
  - 4) The fair values of refundable deposits and guarantee deposits are their carrying values.
  - 5) The fair values of long-term loans equal their carrying values because the interest rate for long-term loans is floating.
- c. Fair values of financial assets and liabilities based on quoted market prices or valuation techniques were as follows:

	<b>Quoted Market Prices</b>		<b>Valuation Techniques</b>	
	<b>December 31</b>		<b>December 31</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
Assets				
Available-for-sale financial assets - noncurrent	\$ 1,161,753	\$ 1,205,266	\$ -	\$ -
Financial assets at FVTPL - current	-	-	3,164	4,586
Financial assets at FVTPL - noncurrent	-	-	259	23,979
Liabilities				
Financial liabilities at FVTPL - current	-	-	3,737	-
Financial liabilities at FVTPL - noncurrent	-	-	1,739	-

- d. As of December 31, 2012 and 2011, the valuation of financial instruments with fair values determined using valuation techniques resulted in a gain of NT\$17,686 thousand and NT\$28,284 thousand, respectively.
- e. As of December 31, 2012 and 2011, financial instruments exposed to cash flow interest rate risk were, financial assets in the amounts of NT\$319,095 thousand and NT\$374,239 thousand, respectively, and financial liabilities in the amounts of NT\$19,675,259 thousand and NT\$18,174,896 thousand, respectively.
- f. As of December 31, 2012 and 2011, the interest income (expense) associated with financial assets (liabilities) other than those at fair value through profit or loss was as follows:

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
Total interest income	\$ 1,383	\$ 1,377
Total interest expense (including capitalized interest)	264,942	163,671

g. Financial risk

1) Market risk

This includes fair value risk on interest rate, exchange rate and market prices. The Corporation's investment in the shares of China Steel Corporation (CSC) involves market risk, i.e., if CSC's share price increases or decreases by NT\$1.00, fair value will increase or decrease by NT\$42,477 thousand.

2) Credit risk

Credit risk represents the potential loss that would be incurred by the Corporation if the counterparties or third-parties breach the contracts. Factors affecting credit risk are credit risk concentration, instrument components, contract amounts and other receivables.

As of December 31, 2012, the Corporation's credit risks amounted to NT\$1,342,914 thousand (including accounts receivable, receivables from related parties, other receivables, other receivables from related parties and refundable deposits), and the maximum credit risk on the instruments and the carrying value of these instruments are the same. The credit risk on the Corporation's cash and bank deposits (including pledged time deposits) were considered insignificant.

3) Liquidity risk

The Corporation had a deficit in 2012. Although the Corporation's current liabilities exceeded current assets as of December 31, 2012, the Corporation's operating funds were deemed sufficient to meet cash flow demand because of acquisition of short and long term loans. Thus, liquidity risk was not considered significant.

In addition, available-for-sale financial assets can be readily sold at prices approximating fair values. There are liquidity risks, however, for financial assets carried at cost because they have no active market.

4) Cash flow risk on interest rate changes

The Corporation's short-term and long-term loans are floating-rate loans. When the market interest rate increases by 1%, the Corporation's cash outflow will increase by about NT\$196,753 thousand a year.

## 23. RELATED-PARTY TRANSACTIONS

### a. Related parties

<u>Related Party</u>	<u>Relationship with the Corporation</u>
China Steel Corporation (CSC)	Major stockholder (41%)
Long-Yuan-Fa Investment Corporation (LYFIC)	Affiliate (re-elected and dismissed supervisor of the Corporation on June 13, 2012)
Hong-Yih Investment Corporation (HYIC)	Affiliate (re-elected and dismissed director of the Corporation on June 13, 2012)
Goang Yaw Investment Corporation (GYIC)	Affiliate (re-elected and dismissed director of the Corporation on June 13, 2012)
Pacific Harbour Stevedoring Corp. (PHSC)	Serves as director and supervisor
Cheng Shin House Management Consulting Corp. (CSHMCC)	Serves as director
Hung Li Steel Corporation (HLC)	Subsidiary
Taiwan Steel Corporation (TSC)	Subsidiary with no significant transaction
Hong Kao Investment Corporation (HKIC)	Subsidiary with no significant transaction
Transglory Investment Corporation (TIC)	Equity-method investee
China Steel Global Trading Corporation (CSGC)	Affiliate
Dragon Steel Corporation (DSC)	Affiliate
Infor-Champ Systems Corporation (ICSC)	Affiliate
China Ecotek Corporation (CEC)	Affiliate
China Steel Machinery Corporation (CSMC)	Affiliate
China Hi-ment Corporation (CHC)	Affiliate
Steel Castle Technology Corporation (SCT)	Affiliate
China Steel Security Corporation (CSS)	Affiliate
China Steel Structure Corporation (CSSC)	Affiliate
United Steel Engineering and Construction Corporation (USECC)	Affiliate
United Steel Development Co., Ltd. (USDCL)	Affiliate
Universal Exchange Inc. (UEI)	Affiliate
Union Steel Development Corporation (USDC)	Affiliate
Hi-mag Magnetic Corporation (HMC)	Affiliate
China Steel Management Consulting Corporation (CSMCC)	Affiliate
China Steel Corporation Group Education Foundation (CSCGEF)	Corporation is the main donor
CSC Steel SDN. BHD. (CSSB)	Affiliate
CSGT Steel Vietnam Joint Stock Company (CSGT METALS)	Affiliate

b. Significant related-party transactions were as follows:

	<b>Years Ended December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
1) Sale of steel products				
HLC	\$ 2,742,823	6	\$ 3,323,224	7
CSSB	231,523	1	742,945	2
CSGT METALS	52,486	-	131,099	-
Others	<u>13,548</u>	<u>-</u>	<u>13,881</u>	<u>-</u>
	<u>\$ 3,040,380</u>	<u>7</u>	<u>\$ 4,211,149</u>	<u>9</u>

The selling prices of steel products for related parties were similar to those for third parties. However, CSSB and CSGT METALS paid by telegraphic transfers (T/T) within seven days from product shipment, and these payment terms differed from those for third parties, from whom payments were collected in advance.

	<b>Years Ended December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
2) Service revenue				
CSC	\$ 91,268	96	\$ 113,566	91
HLC	<u>2,000</u>	<u>2</u>	<u>2,250</u>	<u>2</u>
	<u>\$ 93,268</u>	<u>98</u>	<u>\$ 115,816</u>	<u>93</u>

The Corporation entered into an agreement with CSC for the Corporation to do certain processing work on CSC's steel products. The calculation of processing charges to CSC was based on the formula stated in the agreement. The Corporation bills CSC within one month after approval of delivery.

The Corporation entered into an agreement with HLC to be a sales agent for its products and received service compensation every month. As of December 31, 2012 and 2011, the receivables from third parties of NT\$15,544 thousand and NT\$66,768 thousand were recognized as other receivables and the payables to HLC of NT\$76,375 thousand and NT\$63,342 thousands were recognized as other payables.

	<b>Years Ended December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
3) Sale of supplies (recorded in other operating revenues)				
DSC	\$ 31,906	99	\$ -	-
HLC	<u>-</u>	<u>-</u>	<u>5,549</u>	<u>100</u>
	<u>\$ 31,906</u>	<u>99</u>	<u>\$ 5,549</u>	<u>100</u>

	<b>Years Ended December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
4) Purchase of materials				
CSC	\$ 3,776,199	11	\$ 2,908,533	7
DSC	<u>3,013,037</u>	<u>9</u>	<u>4,357,229</u>	<u>10</u>
	<u>\$ 6,789,236</u>	<u>20</u>	<u>\$ 7,265,762</u>	<u>17</u>

Payment terms for purchases of materials were similar to those for normal purchases from third parties. The amount of purchase from DSC included purchases from CSC through DSC.

#### 5) Deferred credits

In July, 2009, Taiwan Kaohsiung District Court (TKDC) auctioned off JAS's collaterals, and HLC bid for them. In November, 2009, TKDC allocated the proceeds of the auction of JAS's collaterals, with the Corporation getting the largest allocation.

As a result of the transaction, the gain on disposal of nonperforming loans decreased to NT\$1,257,034 thousand in 2009. In addition, some of the collaterals went to HLC, a subsidiary of the Corporation; thus, the gain was reclassified to deferred credits and was recognized on the basis of its realization period (which is HLC's property depreciation period).

Related information on the deferred credits is as follows:

	<b>2012</b>	<b>2011</b>
Balance, beginning of year	\$ 1,068,844	\$ 1,150,987
Realized gain	<u>(82,142)</u>	<u>(82,143)</u>
Balance, end of year	<u>\$ 986,702</u>	<u>\$ 1,068,844</u>

The realized gain on nonperforming loans was included in "others" of nonoperating income and gains.

#### 6) Authorization fees

In May 2003, CSC, Sumitomo Metal Industries, Ltd. (SMI) and Sumitomo Corporation (SC) entered into a joint venture agreement and established a holding company named East Asia United Steel Corporation (EAUS) in July 2003. CSC will have a stable supply of good quality slab through this joint venture. CSC then signed a contract with the Corporation, transferring to the Corporation the right to buy slab from EAUS. The Corporation should pay authorization fees of US\$6.00 per ton to CSC. These fees (included in the purchase of materials) were NT\$315,590 thousand in 2012 and NT\$324,593 thousand in 2011. As of December 31, 2012 and 2011, authorization fees payable (included in payables to related parties) were NT\$82,328 thousand and NT\$85,692 thousand, respectively. The calculation of slab purchase prices was based on the formula stated in the agreement.

7) Lending and returning of steel slabs

To maintain steel slabs for production, the Corporation entered into a contract with CSC and DSC, under which the Corporation can borrow slabs from CSC and DSC when the Corporation needs more production materials and then return the slabs to CSC and DSC when the Corporation has a surplus of materials. The borrowing and returning of steel slabs in 2012 and 2011 are summarized as follows:

	(Unit: Ton)		
	CSC	DSC	Total
<u>2012</u>			
Balance, beginning of year	9,252	-	9,252
Lending for the year	59,871	74,593	134,464
Returns for the year	(59,394)	(73,781)	(133,175)
Allowance for inventory loss	<u>(6,094)</u>	<u>(812)</u>	<u>(6,906)</u>
Balance, end of year	<u>3,635</u>	<u>-</u>	<u>3,635</u>
<u>2011</u>			
Balance, beginning of year	37,045	-	37,045
Lending for the year	190,372	-	190,372
Returns for the year	(215,033)	(49,459)	(264,492)
Allowance for inventory loss	<u>(3,132)</u>	<u>49,459</u>	<u>46,327</u>
Balance, end of year	<u>9,252</u>	<u>-</u>	<u>9,252</u>

According to the contract with DSC, the Corporation should pay DSC when it borrows steel slabs from DSC. And the Corporation collects the money back when it returns the borrowed slabs to DSC. As of December 31, 2012 and 2011, all liabilities were discharged in both years.

8) Processing charge

The Corporation authorized HLC to do some steel processing in the amounts of to NT\$368,196 thousand and NT\$370,051 thousand in 2012 and 2011. As of December 31, 2012 and 2011, the processing payable was NT\$10,893 thousand and NT\$30,952 thousand, included in accrued expenses.

9) Construction- in-progress and other expenditures

Other expenditures paid to related parties, which pertained to construction or maintenance, were as follows:

	Years Ended December 31			
	2012		2011	
	Other Expenditures	Construction- In-progress	Other Expenditures	Construction- In-progress
PHSC	\$ 172,842	\$ -	\$ 187,606	\$ -
CSGC	71,383	-	64,028	-
CSMC	14,509	-	20,111	-
CSC	14,474	6,138	46,537	262

(Continued)

	<b>Years Ended December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Other Expenditures</b>	<b>Construction-In-progress</b>	<b>Other Expenditures</b>	<b>Construction-In-progress</b>
ICSC	\$ 11,812	\$ 142,751	\$ 5,770	\$ 51,368
USECC	4,114	99,422	2,139	-
CEC	88	28,999	-	35,045
CSSC	-	154,431	-	-
USDCL	-	70,731	-	-
Others	<u>33,451</u>	<u>-</u>	<u>28,730</u>	<u>1,119</u>
	<u>\$ 322,673</u>	<u>\$ 502,472</u>	<u>\$ 354,921</u>	<u>\$ 87,794</u>

(Concluded)

10) Income from supplies and scrap

	<b>Years Ended December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
CHC	\$ 387,296	39	\$ 436,034	37
CSGC	58,957	6	56,581	5
Others	<u>7,905</u>	<u>-</u>	<u>4,254</u>	<u>-</u>
	<u>\$ 454,158</u>	<u>45</u>	<u>\$ 496,869</u>	<u>42</u>

c. Balances at year-end

	<b>December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
1) Accounts receivable				
CSC	\$ 12,333	1	\$ 22,853	3
HLC	-	-	140,038	15
CSSB	-	-	20,768	2
Others	<u>3,139</u>	<u>-</u>	<u>2,858</u>	<u>-</u>
	<u>\$ 15,472</u>	<u>1</u>	<u>\$ 186,517</u>	<u>20</u>
2) Notes payable				
USECC	\$ 1,595	6	\$ -	-
ICSC	1,405	5	-	-
Others	<u>1,070</u>	<u>4</u>	<u>-</u>	<u>-</u>
	<u>\$ 4,070</u>	<u>15</u>	<u>\$ -</u>	<u>-</u>

(Continued)

	<b>December 31</b>			
	<b>2012</b>		<b>2011</b>	
	<b>Amount</b>	<b>% to Total</b>	<b>Amount</b>	<b>% to Total</b>
3) Accounts payable				
CSC	\$ 233,931	16	\$ 135,031	11
Others	<u>9,996</u>	<u>1</u>	<u>1,427</u>	<u>-</u>
	<u>\$ 243,927</u>	<u>17</u>	<u>\$ 136,458</u>	<u>11</u>
4) Other receivable				
CSC	\$ 143,518	72	\$ 6,387	5
CHC	31,932	16	34,783	28
Others	<u>3,072</u>	<u>2</u>	<u>3,242</u>	<u>2</u>
	<u>\$ 178,522</u>	<u>90</u>	<u>\$ 44,412</u>	<u>35</u>

(Concluded)

d. Compensation of directors, supervisors and management personnel

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
Salaries	\$ 20,292	\$ 17,152
Special compensation	768	360
Incentives	<u>5,883</u>	<u>6,413</u>
	<u>\$ 26,943</u>	<u>\$ 23,925</u>

## 24. PLEDGED ASSETS

Assets pledged or mortgaged as collateral for bank loans were as follows:

	<b>December 31</b>	
	<b>2012</b>	<b>2011</b>
Properties, net	\$ 8,438,791	\$ 9,137,211
Restricted assets - time deposits	<u>300,000</u>	<u>300,000</u>
	<u>\$ 8,738,791</u>	<u>\$ 9,437,211</u>

## 25. SIGNIFICANT COMMITMENTS AND CONTINGENCIES AS OF DECEMBER 31, 2012

- a. Unused letters of credit for purchases of raw materials and machinery and equipment amounted to about NT\$3,237,090 thousand.
- b. The Corporation had signed agreements to buy equipment for NT\$3,442,646 thousand, of which NT\$1,261,298 thousand had been paid (included in construction-in-progress and prepayments for equipment).

- c. The Corporation had signed contracts with foreign suppliers to buy slabs to ensure sufficiency of production materials. Unpaid purchase amounts for 200,000 tons of slabs as of December 31, 2012 were NT\$2.7 billion. The purchase price plus processing costs of some contracts will be higher than the net realizable value; the variances in losses on purchase contracts payable were as follows:

	<b>Years Ended December 31</b>	
	<b>2012</b>	<b>2011</b>
Balance, beginning of year	\$ 574,800	\$ 246,417
Recognized for the year	846,325	1,579,220
Deducted for the year	<u>(1,421,125)</u>	<u>(1,250,837)</u>
Balance, end of year	<u>\$ -</u>	<u>\$ 574,800</u>

- d. Authorization fee is described in Note 23.
- e. The lease contract of Kaohsiung Long Dong Section is described in Note 11.

## 26. EXCHANGE RATE INFORMATION OF FOREIGN- CURRENCY FINANCIAL ASSETS AND LIABILITES

The significant foreign-currency financial assets and liabilities were as follows:

	<b>December 31</b>					
	<b>2012</b>			<b>2011</b>		
	<b>Foreign Currencies Amount (Thousands)</b>	<b>Exchange Rate</b>	<b>NTD Amount (Thousands)</b>	<b>Foreign Currencies Amount (Thousands)</b>	<b>Exchange Rate</b>	<b>NTD Amount (Thousands)</b>
Monetary Financial Assets						
USD	\$ 27,593	29.04	\$ 801,313	\$ 19,295	30.275	\$ 584,158
Monetary Financial Liabilities						
USD	56,361	29.04	1,636,742	38,572	30.275	1,167,791

## 27. OPERATING SEGMENT FINANCIAL INFORMATION

In accordance with Statement of Financial Accounting Standards No. 41, the Corporation disclosed its operating segment information in the consolidated financial statements as of and for the years ended December 31, 2012 and 2011.

## 28. ADDITIONAL FOOTNOTE DISCLOSURES

As stated in Note 2, additional footnote disclosures that are required by the Securities and Futures Bureau for their oversight purposes but are not required under generally accepted accounting principles were not translated into English from the Chinese version.