CHUNGHWA TELECOM CO LTD
Form 20-F
April 22, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

(Mark One)

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

x **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
for the fiscal year ended December 31, 2012

or

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

or

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

Commission file number 001-31731

Chunghwa Telecom Co., Ltd.

(Exact Name of Registrant as Specified in Its Charter)

Taiwan, Republic of China

(Jurisdiction of Incorporation or Organization)

21-3 Hsinyi Road, Section 1, Taipei, Taiwan, Republic of China

(Address of Principal Executive Offices)

Fufu Shen

21-3 Hsinyi Road, Section 1, Taipei,

Taiwan, Republic of China

Tel: +886 2 2344-5488

Fax: +886 2 3393-8188

(Name, Telephone, email and/or Facsimile number and Address of Company Contact Person)

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

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

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

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

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

7,757,446,545 Common Shares

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ¨ Yes ¨ No

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

Large accelerated filer x Accelerated filer ¨

Non-accelerated filer ¨

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP ¨ International Financial Reporting Standards as issued by the International Accounting Standards Board ¨ Other x

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. ¨ Item 17 x Item 18

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

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

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CHUNGHWA TELECOM CO., LTD.

FORM 20-F ANNUAL REPORT

FISCAL YEAR ENDED DECEMBER 31, 2012

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SUPPLEMENTAL INFORMATION

All references to we, us, our and our company in this annual report are to Chunghwa Telecom Co., Ltd. and our consolidated subsidiaries, unles the context otherwise requires. All references to shares and common shares are to our common shares, par value NT$10 per share, and to ADSs are to our American depositary shares, each of which represents ten of our common shares. The ADSs are issued under the deposit agreement, as amended, supplemented or modified from time to time, originally dated as of July 17, 2003, among Chunghwa Telecom Co., Ltd. and the Bank of New York, and amended and restated on November 14, 2007, among Chunghwa Telecom Co., Ltd. and JP Morgan Chase Bank, as depository, and the holders and beneficial owners of American Depositary Receipts issued thereunder. All references to Taiwan are to the island of Taiwan and other areas under the effective control of the Republic of China. All references to the government or the government of the Republic of China are to the government of the Republic of China. All references to the Ministry of Transportation and Communications are to the Ministry of Transportation and Communications of the Republic of China. All references to the Securities and Futures Bureau are to the Securities and Futures Bureau of the Republic of China or its predecessors, as applicable. ROC GAAP means the generally accepted accounting principles of the Republic of China, and U.S. GAAP means the generally accepted accounting principles of the United States. Any discrepancies in any table between totals and sums of the amounts listed are due to rounding. Unless otherwise indicated, or the context otherwise requires, references in this annual report to financial and operational data for a particular year refer to the fiscal year of our company ending December 31 of that year.

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

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

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

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

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

These forward-looking statements are generally indicated by the use of forward-looking terminology such as believe, expect, anticipate, estimate, plan, aim, seek, project, may, will or other similar words that express an indication of actions or results of actions that may o expected to occur in the future. These statements reflect our current views with respect to future events and are subject to risks, uncertainties and assumptions, many of which are beyond our control. The forward-looking statements are contained principally in the sections entitled Item 3. Key Information D. Risk Factors, Item 4. Information on the Company and Item 5. Operating and Financial Review and Prospects . These statements are made under the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. You should not place undue reliance on these statements, which apply only as of the date of this annual report. These forward-looking statements are based on our own information and on information from other sources we believe to be reliable. Actual results may differ materially from those expressed or implied by these forward-looking statements. Factors that could cause differences include, but are not limited to, those discussed under Item 3. Key Information D. Risk Factors . In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this annual report might not occur and our actual results could differ materially from those anticipated in these forward-looking statements. The forward-looking statements made in this annual report relate only to events or information as of the date on which the statements are made in this annual report. Except as required by law, we undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise, after the date on which the statements are made or to reflect the occurrence of unanticipated events. You should read this annual report completely and with the understanding that our actual future results may be materially different from what we expect.

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PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

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

A. Selected Financial Data

The selected income statement data and cash flow data for the years ended December 31, 2010, 2011 and 2012, and the selected balance sheet data as of December 31, 2011 and 2012 set forth below are derived from our consolidated financial statements included elsewhere in this annual report and should be read in conjunction with, and are qualified in their entirety by reference to, our consolidated financial statements and the related notes. The selected income statement and cash flow data for the years ended December 31, 2008 and 2009, and the selected balance sheet data as of December 31, 2008, 2009 and 2010 set forth below, are derived from our consolidated financial statements not included in this annual report. The consolidated financial statements have been prepared and presented in accordance with accounting principles generally accepted in the Republic of China, or ROC GAAP, which differ in some material respects from accounting principles generally accepted in the United States of America, or U.S. GAAP, as further explained under note 34 to our consolidated financial statements included herein.

	Year Ended December 31,					
	2008	2009	2010	2011	2012	
	NT$	NT$	NT$	NT$	NT$	US$
	(in billions, except for percentages and per share and per pro forma ADS data)					
Income Statement Data:						
ROC GAAP						
Net revenues	201.7	198.4	202.4	217.5	220.1	7.6
Operating costs	(113.5)	(112.7)	(115.3)	(131.5)	(141.2)	(4.9)
Gross profit	88.2	85.7	87.1	86.0	78.9	2.7
Operating expenses	(29.6)	(29.3)	(29.7)	(30.9)	(30.0)	(1.0)
Income from operations	58.6	56.4	57.4	55.1	48.9	1.7
Non-operating income and gains(1)	3.4	1.4	1.0	1.9	1.9	0.1
Non-operating expenses and losses(1)	(2.3)	(0.6)	(0.7)	(0.3)	(1.9)	(0.1)

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	Year Ended December 31,					
	2008	2009	2010	2011	2012	
	NT$	NT$	NT$	NT$	NT$	US$
	(in billions, except for percentages and per share and per pro forma ADS data)					
Income before income tax	59.7	57.2	57.7	56.7	48.9	1.7
Income tax expense[2]	(13.9)	(12.7)	(9.1)	(8.6)	(7.9)	(0.3)
Consolidated net income	45.8	44.5	48.6	48.1	41.0	1.4
Attributable to:						
Stockholders of the parent	45.0	43.8	47.6	47.1	39.9	1.4
Minority interests	0.8	0.7	1.0	1.0	1.1	
	45.8	44.5	48.6	48.1	41.0	1.4
Earnings per share:						
Basic	4.64	4.51	4.91	6.04	5.14	0.18
Diluted	4.63	4.50	4.89	6.03	5.13	0.18
Earnings per ADS equivalent:						
Basic	46.42	45.16	49.10	60.43	51.44	1.77
Diluted	46.31	45.01	48.95	60.25	51.30	1.77
U.S. GAAP						
Net revenues	204.4	200.4	203.8	218.3	220.7	7.6
Operating costs and expenses	(147.1)	(141.8)	(145.2)	(161.2)	(170.8)	(5.9)
Income from operations	57.3	58.6	58.6	57.1	49.9	1.7
Non-operating income, net[1]	1.4	0.8	0.6	1.3		
Income before income tax	58.7	59.4	59.2	58.4	49.9	1.7
Income tax expense[2]	(14.5)	(13.6)	(10.0)	(9.0)	(7.3)	(0.2)
Consolidated net income	44.2	45.8	49.2	49.4	42.6	1.5
Attributable to:						
Stockholders of the parent	43.7	45.1	48.3	48.4	41.5	1.4
Noncontrolling interests	0.5	0.7	0.9	1.0	1.1	0.1
	44.2	45.8	49.2	49.4	42.6	1.5
Earnings per share:						
Basic	4.52	4.65	4.98	6.22	5.34	0.18
Diluted	4.51	4.64	4.96	6.20	5.33	0.18
Earnings per ADS equivalent:						
Basic	45.19	46.51	49.78	62.17	53.43	1.84
Diluted	45.09	46.36	49.64	62.00	53.29	1.83

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	As of December 31,					
	2008	2009	2010	2011	2012	
	NT$	NT$	NT$	NT$	NT$	US$
	(in billions, except for percentages and per share and per pro forma ADS data)					
Balance Sheet Data:						
ROC GAAP						
Working capital	48.3	54.8	48.5	47.3	44.2	1.5
Long-term investments	8.9	9.1	13.9	19.9	20.8	0.7
Properties	323.0	313.0	305.7	302.6	303.7	10.5
Goodwill	0.2	0.3	0.3	0.2	0.2	
Total assets	463.6	449.0	454.3	442.9	439.4	15.1
Short-term loans	0.3	0.8	0.1	0.1	0.1	
Short-term bills payable			0.2			
Current portion of long-term loans		0.1	0.3	0.7		
Long-term loans[3]		0.2	3.1	1.1	2.1	0.1
Deferred income	2.1	2.5	2.6	2.6	2.7	0.1
Other liabilities	11.8	7.5	7.5	6.9	7.9	0.3
Total liabilities	83.9	70.0	85.7	69.9	69.5	2.4
Capital stock	97.0	97.0	77.6	77.6	77.6	2.7
Cash dividend on common shares	40.7	37.1	39.4	42.9	42.4	1.5
Equity attributable to stockholders of the parent	376.6	375.2	364.6	368.7	365.4	12.6
Minority interests in subsidiaries	3.1	3.8	4.0	4.3	4.5	0.1
U.S. GAAP						
Total assets	400.7	385.4	390.5	379.4	376.3	12.9
Total liabilities	94.8	78.9	94.4	78.0	76.6	2.6
Capital stock	97.0	97.0	77.6	77.6	77.6	2.7
Equity attributable to stockholders of the parent	302.8	302.8	292.2	297.3	295.4	10.2
Noncontrolling interests	3.1	3.7	3.9	4.1	4.3	0.1

	Year Ended December 31,					
	2008	2009	2010	2011	2012	
	NT$	NT$	NT$	NT$	NT$	US$
	(in billions, except for percentages and per share and per pro forma ADS data)					
Cash Flow Data:						
ROC GAAP						
Net cash provided by operating activities	91.9	77.3	84.8	75.3	67.5	2.3
Net cash used in investing activities	(34.5)	(29.5)	(17.4)	(33.1)	(38.9)	(1.3)
Net cash used in financing activities	(52.3)	(56.5)	(47.0)	(65.7)	(42.8)	(1.5)
Net increase (decrease) in cash and cash equivalents	5.1	(8.0)	17.6	(23.5)	(14.2)	(0.5)
Other Financial Data:						
ROC GAAP						
Gross margin[4]	44%	43%	43%	39%	36%	36%
Operating margin[5]	29%	28%	28%	25%	22%	22%
Net margin[6]	22%	22%	24%	22%	18%	18%
Capital expenditures	30.1	25.5	24.6	26.9	33.3	1.1
Depreciation and amortization	38.2	36.3	34.1	32.3	32.5	1.1
Cash dividends declared per share	3.83 [7]	4.06 [7]	5.52 [7]	5.46 [7]	[8]	[8]
Stock dividends declared per share	1.00				[8]	[8]

(1) Includes interest income of NT$1,916 million, NT$479 million, NT$475 million, NT$682 million and NT$742 million (US$25.5 million) for the years ended December 31, 2008, 2009, 2010, 2011 and 2012 respectively, and interest expense of NT$4 million, NT$15 million, NT$107 million, NT$31 million and NT$22 million (US$0.8 million) for the years ended December 31, 2008, 2009, 2010, 2011 and 2012 respectively.

(2) In May 2009, the Legislative Yuan passed an amendment to Article 5 of the Income Tax Law, which reduces the income tax rate of profit-seeking enterprises from 25% to 20%, effective in 2010. Furthermore, in May 2010, the Legislative Yuan passed the amendment to Article 5 of the Income Tax Law, which reduced the income tax rate of profit-seeking enterprises from 20% to 17%, effective retroactively from January 1, 2010.

(3) Excludes current portion of long-term loans.

(4) Represents gross profits divided by net revenues.

(5) Represents income from operations divided by net revenues.

(6) Represents net income attributed to stockholders of the parent divided by net revenues.
(7) Dividends for 2008, 2009, 2010 and 2011 in U.S. dollars were US$0.12, US$0.14, US$0.18 and US$0.19, respectively. The amounts were calculated using the exchange rates of the subsequent years for convenience translation.
(8) Dividends for 2012 have not yet been declared by the board of directors and are expected to be declared at our annual general stockholders meeting scheduled for June 25, 2013.

Currency Translations and Exchange Rates

For the convenience of readers, NT dollar amounts used in this annual report for, and as of, the year ended December 31, 2012 have been translated into U.S. dollar amounts using US$1.00=NT$ 29.05, set forth in the statistical release of the Federal Reserve Board on December 31, 2012. The U.S. dollar translation appears in parentheses next to the relevant NT dollar amount. We make no representation that any New Taiwan dollar amounts or U.S. dollar amounts referred to in this annual report could have been or could be converted into U.S. dollars or NT dollars, as the case may be, at any particular rate or at all. On April 12, 2013, the exchange rate was NT$29.95 to US$1.00.

The following table sets forth, for each of the periods indicated, the low, average, high and period-end exchange rates of the NT dollar, expressed in NT dollar per U.S. dollar. These rates are provided solely for your convenience and are not necessarily the exchange rates that we used in this annual report or will use in the preparation of our periodic reports or any other information to be provided to you.

Year Ended December 31,	Average(1)	High	Low	At Period End
2008	31.51	33.58	29.99	32.76
2009	33.02	35.21	31.95	31.95
2010	31.50	32.43	29.14	29.14
2011	29.42	30.67	28.50	30.27
2012	29.56	30.27	28.96	29.05
October	29.24	29.31	29.15	29.20
November	29.11	29.26	28.96	29.07
December	29.04	29.10	29.00	29.05
2013 (through April 12)	29.74	30.06	28.93	29.95
January	29.10	29.54	28.93	29.54
February	29.63	29.73	29.52	29.67
March	29.75	29.88	29.63	29.81
April (through April 12)	29.94	30.06	29.86	29.95

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

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

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

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

Risks Relating to Our Company and the Taiwan Telecommunications Industry

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

As a telecommunications service provider in Taiwan, we are subject to extensive regulation. See Item 4. Information on the Company B. Business Overview Regulation for a discussion of the regulatory environment applicable to us. Any changes in the regulatory environment applicable to us may adversely affect our business, financial condition and results of operations.

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For example, the National Communications Commission, or the NCC, submitted a proposal to the Executive Yuan on July 30, 2012 for an amendment to the Telecommunications Act. This proposed amendment includes several provisions made against the operation of dominant telecommunication service providers, such as the mandatory segregation of financial data, price control, separation between the underlying network infrastructure and services provision of the last-mile technology and the requirement for dominant providers to release local loops and provide relevant sharing services. These requirements would allow all telecommunications service providers to have access to our last-mile network infrastructure. The above proposal was later returned by the Executive Yuan to the NCC on October 5, 2012 for consideration, and the NCC will submit an alternative proposed amendment to the Executive Yuan. We believe the amendment will still take a strict approach on dominant operators and may have a material impact on us once approved.

On the other hand, the Legislative Yuan is reviewing the proposed amendments to the three applicable regulations governing broadcasting industries for relaxing the current restrictions regarding investments in the broadcasting industries by the government and political parties. Pursuant to these amendments, the government may indirectly hold shares in broadcasting companies, provided that the government s shareholding is no more than 10% and the government does not control such companies. As the Ministry of Transportation and Communications, or MOTC, holds more than 30% of our shares and retains control over our board, such amendments will not release the current restrictions on us with respect to engaging in the broadcasting business. However, these amendments may benefit our competitors, which could have a material adverse effect on our business prospects and results of operations.

We have been designated by the government as a dominant provider of fixed communications and mobile services within the meaning of applicable telecommunications regulations, and as a result, we are subject to special additional requirements imposed by the NCC. For example, the regulation governing the setting and changing of tariffs allows non-dominant telecommunications service providers greater freedom to set and change tariffs within the range set by the government. If we are unable to respond effectively to tariff changes by our competitors, then our competitiveness, market position and profitability will be materially and adversely affected. According to the Fixed Network Regulations, we are required to submit a report to the NCC within 20 days after our shareholders approve the entering into, modification or termination of any contracts regarding leasing of all business, outsourcing of operations or joint operations, the transfer of the whole or substantial part of our business or assets; and taking over of the whole of the business or assets of any other company which would have significant impact on our operations. The NCC also amended the Wireless Regulations and the Third Generation Mobile Telecommunications Services Regulations on April 3, 2009 to impose a similar requirement requiring us to submit a report within 20 days after our shareholders approve one of the above matters or our capital reduction. We were subject to the Statute of Chunghwa Telecom Co., Ltd. prior to our privatization. Although we have been privatized, the Legislative Yuan has not yet abolished the Statute of Chunghwa Telecom Co., Ltd., and at this time, the Statute of Chunghwa Telecom Co., Ltd. is still applicable to us. Under the Statute of Chunghwa Telecom Co., Ltd., the Ministry of Transportation and Communications has the authority to regulate some aspects of our business. Any such regulation could be burdensome or conflict with regulations of the NCC or may otherwise adversely affect our business, financial condition and results of operations.

The regulatory framework within which we operate may limit our flexibility to respond to market conditions, competition or changes in our cost structure. In particular, future decreases in tariff rates could immediately and substantially decrease our revenues. In particular, as a Type I service provider under the Republic of China Telecommunications Act, or Telecommunications Act, we are constrained in our ability to raise prices. For example, the NCC adopted the first three-year tariff reduction plan from April 2007 to March 2010 and a second three-year tariff reduction plan from April 2010 to March 2013, resulting in a number of price reductions in the tariff structures relating to our domestic fixed communications and mobile communications services. On February 7, 2013, the NCC announced a new plan for tariff reductions in wholesale tariffs for IP peering and domestic leased line services, and in monthly fees for fixed-line broadband services (excluding fiber-to-the-home, or FTTH, and fiber-to-the-building, or FTTB) over a period of four years starting on April 1, 2013. While mobile tariffs were not regulated in the most recent tariff reduction plan, the revised Administrative Rules for Network Interconnection mandated decreases in the mobile interconnection fees over a period of four years starting on January 5, 2013. In addition, each operator was required by the NCC to submit a mobile voice service tariffs reduction plan along with the interconnection rate reduction plan, and the new decreased mobile voice service tariffs became effective on April 1, 2013. See Item 5. Operating and Financial Review and Prospects Overview Tariff adjustments . We cannot assure you that we will not be required to further reduce our tariffs again in the future. Any mandatory tariff reductions could have a material adverse effect on our revenues.

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If we fail to comply with the regulations of the ROC Fair Trade Act, we may be investigated and fined.

As a provider of telecommunication products and services, our business operations are subject to the regulations of the ROC Fair Trade Act, or the FTA, which is administered and enforced by the ROC Fair Trade Commission, or the FTC. The FTA requires, among other things, that the marketing and promotional materials of a business to be true and not misleading. The FTA also prohibits a business from participating or engaging in a cartel or other anti-competitive conduct. The FTC has the authority under the FTA to investigate and, where appropriate, impose fines and penalties on a business that violates any regulations promulgated by the FTA. The consequences of any such violations could have a material adverse effect on our business and results of operations. See Item 4. Information on the Company B. Business Overview Regulation for a discussion of the FTA applicable to us. We have been investigated and penalized by the FTC in the past and may continue to be investigated or penalized by the FTC in the future if we fail to comply with the relevant regulations. As the FTA provides the FTC broad discretion to interpret anti-competition actions and enforce the relevant clauses under the FTA, we are unable to predict whether the FTC would initiate investigation on any of our daily business activities or find us liable for violating the FTA in the future. The investigations of and penalties imposed by the FTC could interrupt our provision of products or services and have a negative impact on our reputation, business operations and results of operations.

If we are unable to obtain and maintain the licenses to operate our business, our business prospects and future results of operations would be adversely affected.

We operate our businesses with approvals and licenses granted by the government. If these approvals or licenses are revoked or suspended or are not renewed, or if we are unable to obtain any additional licenses that we may need to operate or expand our business in the manner we desire, then our financial condition and results of operations, as well as our prospects, will suffer. For example, there are currently three mobile network operators that offer 2G mobile services in Taiwan. The licenses granted by the ROC government authorities for operating 2G mobile services on the 900MHz and 1800MHz spectrum can be extended to June 2017 based on the operator s request for extension, according to the Executive Yuan s announcement on November 22, 2010. On November 29, 2011, we filed a request with the NCC to extend our 2G license to June 2017, which was approved by the NCC on November 14, 2012. The NCC announced that it will publish the regulations for the 4G license (officially announced as a mobile broadband license by the NCC) auction for technology neutral usage before the end of June 2013 and complete the auction before the end of December 2013. The NCC is expected to allocate 135MHz x 2 spectrum available for the auction. Although we plan to apply for the license and frequency spectrum for 4G/mobile broadband services, we cannot assure you that we will be able to acquire the license and the frequency spectrum we need for our mobile operations in the future. If we are unable to successfully acquire the rights to use the frequency spectrum that we need for our future business operations, our business prospects and future results of operations may be adversely affected, and as a result may lead to a material impact on our business revenues.

Increasing market competition may adversely affect our growth and profitability by causing us to lose customers, charge lower tariffs or spend more on marketing.

Mobile service providers in Taiwan have been offering 3G mobile services for several years. Smart phones with mobile data packages have become popular in recent years. To attract more high-end data users, the major three mobile operators, including us, have adopted comparable promotion packages to attract and maintain customers. We cannot assure you that the intensified market competition will not affect our growth and profitability.

We also face increased broadband competition from cable operators. Cable operators have been using low-priced internet access packages to attract new customers in specific areas and buildings in Taiwan. They have also been upgrading their networks to DOCSIS 3.0 in order to provide higher speed internet access. DOCSIS refers to Data Over Cable Service Interface Specification, which is an international telecommunications standard that permits the addition of high-speed data transfer to an existing cable TV system. To counter these developments, we keep migrating more of our ADSL customers to FTTx services and to provide even higher speed fiber to the home, or FTTH access. The government has mandated the digitization of cable television networks by 2014. In addition, the NCC relaxed the zoning restrictions on service areas for cable operators on July 27, 2012, while cable operators remain subject to the restriction that the market share of any single cable operator cannot exceed 33%. This change will allow cable operators to provide digital cable services throughout Taiwan, including high definition cable TV with more channels as well as high speed cable modem services. As of now, it is still uncertain whether we will be deemed a cable operator and subject to the 33% market share restriction. As a result, we could face increased competition for our broadband access services and multimedia on demand, or MOD, IPTV services. If we are unable to compete successfully with the cable operators for broadband access services and MOD businesses, our results of operations could be impacted.

Many of our competitors are in alliances with leading international telecommunications service providers and have access to financial and other resources or technologies that may not be available to us. Moreover, if the government continues to liberalize the telecommunications market, such as through the issuance of new licenses or establishment of additional networks, our market position and competitiveness could be materially and adversely affected. We cannot guarantee that our measures to address competition will be effective, and therefore our business, financial condition and results of operations may be adversely affected by our competition.

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

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

Taiwan is susceptible to earthquakes and typhoons. However, we do not carry insurance to cover damage caused by earthquakes, typhoons or other natural disasters or any resulting business interruption. Our services are currently carried through our fixed and mobile communications networks, as well as through our transmission networks consisting of optical fiber cable, microwave, submarine cable and satellite transmission links, which could be vulnerable to damage or interruptions in operations due to natural disasters. For example, in 2012, losses on property, plant and equipment arising from natural disasters such as earthquakes and typhoons were approximately NT$7.4 million (US$0.3 million) as recorded in non-operating expenses under ROC GAAP. The occurrence of natural disasters could impact our ability to deliver services and have a negative effect on our results of operations. Furthermore, we might also be liable for losses claimed from our customers that were incurred from our failure to deliver our services. These potential liabilities could also have a material adverse effect on our results of operations.

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

We are from time to time involved in litigation, arbitration or administrative proceedings in the ordinary course of our business. See Item 4. Information on the Company B. Business Overview Legal Proceedings .

We cannot predict the outcome of these proceedings, and we cannot assure you that if a judgment is rendered against us in any or all of these proceedings, our financial condition and results of operations would not be materially and adversely affected.

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

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

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

We have made significant capital investments in our network infrastructure and information technology systems to provide the services we offer. In 2012, we made capital expenditures in our domestic fixed communications of NT$19.6 billion (US$673.0 million), our mobile communications business of NT$7.2 billion (US$249.0 million), our internet business of NT$3.4 billion (US$118.5 million), our international fixed communications business of NT$2.4 billion (US$81.9 million) and our other businesses of NT$0.7 billion (US$23.3 million), respectively. In order to continue to develop our business and offer new and more sophisticated services, we intend to continue to invest in these areas as well as new technologies. The launch of new and commercially viable products and services is important to the success of our business. We expect to continue making substantial capital expenditures to further develop our range of services and products. Commercial acceptance by consumers of the new and more sophisticated services we offer may not occur at the rate or level expected, and we may not be able to successfully adapt these services to effectively and economically meet our customers demand, thus impairing expected return from our investments.

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We cannot assure you that services enabled by the new technologies we are implementing, such as 100Mbps fiber solution and Heterogeneous, or Marco/Micro/Pico/Femto/BBU+RRH/WiFi mobile technology, will be accepted by the public to the extent required to generate an acceptable rate of return. In addition, we could face the risk of unforeseen complications in the deployment of these new services and technologies, and we cannot assure you that we will not exceed our estimate of the necessary capital expenditure to offer such services. New services and technologies may not be developed and/or deployed according to expected schedules or may not achieve commercial acceptance or be cost effective. The failure of any of our services to achieve commercial acceptance could result in additional capital expenditures or a reduction in profitability to the extent we are required under applicable accounting standards to recognize a charge for impairment of assets. Any such charge could materially and adversely affect our financial condition and results of operations.

In 2012, we determined that parts of our land and telecommunication equipment were impaired and recognized an impairment loss of NT1,505 million (US$51.8 million). In 2012, we also recognized impairment losses of NT$4.8 million (US$0.2 million), NT$35 million (US$1.2 million) and NT$20 million (US$0.7 million) for intangible assets, idle assets and other assets, respectively.

We cannot assure you that we will be able to continue to maintain control of and consolidate the results of operations of our minority-owned subsidiary. For example, we consolidate the results of operations of our subsidiary, Senao, because we have control over the board of directors through the support of the largest beneficial shareholder. We cannot assure you that we will be able to continue maintaining control over the board of directors of Senao. See Item 4. Information on the Company B. Business Overview Mobile Communications Business Sales of Mobile Handsets for further discussion of our control of Senao. If we lose control of our minority-owned subsidiary, we will no longer be able to consolidate the results of operations of such subsidiary, which could adversely affect our consolidated results of operations and ability to meet the operating results guidance that we have projected.

We may also from time to time make equity investments in companies, but we cannot assure you of their profitability. We cannot assure you that losses related to our equity investments will not have a material adverse effect on our financial condition or results of operations. In 2012, we recognized other-than-temporary impairment losses of NT$27 million (US$0.9 million) for available-for-sale financial assets due to the decline in market prices, the time of recovery of which we cannot estimate, and of NT$176 million (US$6.1 million) for financial assets carried at cost due to adverse changes in industry conditions and operating performance that were below expectations. We may be required to record additional impairment charges in future periods, which may have a material adverse effect on our financial condition and future results of operations.

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

The Taiwan telecommunications industry has been characterized by rapid increases in the diversity and sophistication of the technologies and services offered. As a result, we expect that we will need to constantly upgrade our telecommunications technologies and services in order to respond to competitive industry conditions and customer requirements. Developments of new technologies have rendered some less advanced technologies unpopular or obsolete. If we fail to develop, or obtain timely access to, new technologies and equipment, or if we fail to obtain the necessary licenses to provide services using these new technologies, we may lose our customers and market share and become less profitable.

In addition, the cost of implementing new technologies, upgrading our networks or expanding capacity could be significant. In particular, we have made and will continue to make substantial capital expenditures in the near future in order to effectively respond to technological changes, such as the continued expansion of our fiber optic networks and High Speed Packet Access, or HSPA, and HSPA+, and Dual cell HSPA+ mobile network. Furthermore, the 4G/mobile broadband licenses are scheduled to be awarded by the end of 2013. Therefore, we expect to devote additional capital expenditure to the network building for Long Term Evolution, or LTE, network. In addition, to meet the increasingly robust high-bandwidth requirements of digital convergence services, we will expand construction of fiber optic networks, including passive optical networks, or PONs, and optical distribution networks, or ODNs. To the extent these expenditures exceed our cash resources, we will be required to seek additional debt or equity financing. Our ability to obtain additional financing on favorable commercial terms will depend on a number of factors. These factors include our financial condition, results of operations, cash flows and the prevailing market conditions in the domestic and international telecommunications industry, the cost of financing and conditions in the financial markets, and the issuance of relevant government and other regulatory approvals. Any inability to obtain funding for our capital expenditures on commercially acceptable terms could jeopardize our expansion plans and materially and adversely affect our business prospects and future results of operations.

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

We are always evaluating new growth opportunities in the broader telecommunications industry and expect to become an Information and Communications Technology, or ICT, service provider. Some of these opportunities involve new services for which there are no proven markets, and may not develop as expected. Our ability to deploy and deliver these services will depend, in many instances, on new but unproven technologies. These new technologies may not perform as expected or generate an acceptable rate of return. In addition, we may not be able to successfully develop new technologies to effectively and economically deliver these services, or be able to compete successfully in the delivery of telecommunications services based on new technologies. Furthermore, the success of our mobile data services is substantially dependent on the availability of mobile data applications and devices that are being developed by third-party developers. These applications or devices may not be sufficiently developed to support the deployment of our mobile data services. If we are unable to deliver commercially viable services based on the new technologies that we adopt, our financial condition and results of operations may be materially and adversely affected.

As an internet service provider, we may not be able to protect our customers and their information from cyber attacks, nor protect our services from disruptions due to cyber security breaches.

As an internet service provider, our system is susceptible to cyber security risks, including hijack attacks, phishing attacks, hacker s intrusions to steal customer s information and distributed denial-of-service (DDoS) attacks. Our online services such as e-bills and multiple payment options through the internet are also vulnerable to cyber attacks. These attacks may disrupt our services and cause leakage of our customers personal information, which may result in significant damage and material adverse effect to our customers and our operations. We cannot assure you that our data protection measures are sufficient to prevent any data leakage or disruption of our service due to cyber attacks. We may suffer negative consequences, such as remedial costs, increased cyber security protection costs, lost revenues, litigation and reputational damage due to cyber attacks.

Our largest stockholder may take actions that conflict with our public stockholders best interests.

As of December 31, 2012, our largest shareholder, the government of the Republic of China, through the Ministry of Transportation and Communications, owned approximately 35.29% of our outstanding common shares. Accordingly, the government, through its control over our board, as all non-independent board members were appointed by the Ministry of Transportation and Communications, may continue to have the ability to control our business, including matters relating to:

- any sale of all or substantially all of our assets;
- the approval of our annual operation and projects budget;
- the composition of our senior management;

- the timing and distribution of dividends;
- the election of a majority of our directors and supervisors; and
- our business activities and direction.

We cannot assure you that our largest shareholder will not take actions that impair our ability to conduct our business competitively or conflict with the best interests of our public stockholders.

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

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

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

We are subject to the reporting requirements of the SEC. The SEC, as directed by Section 404 of the U.S. Sarbanes-Oxley Act of 2002, adopted rules requiring U.S. public companies to include a report of management on our internal control over financial reporting in their annual reports that contain an assessment by management of the effectiveness of our internal control over financial reporting. The effectiveness of our internal control over financial reporting has been audited by Deloitte & Touche, an independent registered public accounting firm, which has also audited our consolidated financial statements for the year ended December 31, 2012. Deloitte & Touche has issued an attestation report on the effectiveness of our internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). See Item 15. Controls and Procedures Attestation Report of the Registered Public Accounting Firm .

While the management report included in this annual report concluded that our internal control over financial reporting was effective, we cannot assure you that our management will be able to conclude that our internal control over financial reporting is effective in future years. If in future years we fail to maintain effective internal control over financial reporting in accordance with the Sarbanes-Oxley Act, we could suffer a loss of investor confidence in the reliability of our consolidated financial statements, which in turn could negatively impact the trading price of our ADSs, result in lawsuits being filed against us by our stockholders or otherwise harm our reputation.

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

In accordance with the articles of association of Chunghwa Telecom Workers Union, besides the chief manager of each department, most of our employees are members of our principal labor union, the Chunghwa Telecom Workers Union. Since our incorporation in 1996, we have experienced disputes with our labor union on such issues as employee benefits and retirement benefits in connection with our privatization as well as the right to protest. Despite having taken measures to improve relations, increase cooperation and ensure mutual benefit with our labor union, such as increasing channels of communications by holding periodic labor resource review meetings and guaranteeing a labor union seat on our board of directors, we cannot assure you that we will be able to maintain a good relationship with our labor union. Any deterioration in our relationship with our labor union could result in work stoppages, strikes or threats to take such an action, which could disrupt our business and operations, materially and adversely affect the quality of our services and harm our reputation.

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

We conduct most of our operations and generate most of our revenues in Taiwan. As a result, any decline in the Taiwan economy or a decline in the growth of the population in Taiwan may materially and adversely affect our financial condition, results of operations and prospects. For example, the global slowdown in technology expenditures has from time to time adversely affected the Taiwan economy, which is highly dependent on the technology industry. The current European debt crisis and related financial restructuring efforts, including in Greece, Italy, Spain, Portugal and Ireland, are contributing to instability in global financial markets, which adversely affects consumer confidence, the cost of borrowing and economic activity, and might also have an impact on the Taiwan economy and hence on our financial condition. Furthermore, there is considerable uncertainty over the long-term effects of the expansionary monetary and fiscal policies that have been adopted by the central banks and financial authorities of some of the world s leading economies. There have also been concerns over unrest in the Middle East and Africa, which has resulted in higher oil prices and significant market volatility, and concerns about the economic effect of the earthquake, tsunami and nuclear crisis in Japan.

As our business is significantly dependent on economic growth, any uncertainty or further deterioration in economic conditions could have a material adverse effect on our financial condition and results of operations. We cannot assure you that economic conditions in Taiwan will continue to improve in the future or that our business and operations will not be materially and adversely affected by deterioration in the Taiwan economy.

We face substantial political risks associated with doing business in Taiwan, particularly due to domestic political events and the tense relationship between the Republic of China and the People s Republic of China, which could adversely affect our financial condition and results of operations.

Our principal executive offices and substantially all of our assets are located in Taiwan, and substantially all of our revenues are derived from our operations in Taiwan. Accordingly, our business, financial condition and results of operations and the market price of our common shares and the ADSs may be affected by changes in Republic of China governmental policies, taxation, inflation or interest rates and by social instability and diplomatic and social developments in or affecting Taiwan which are outside of our control. Taiwan has a unique international political status. Since 1949, Taiwan and the Chinese mainland have been separately governed. The People s Republic of China, or PRC, claims that it is the sole government in China and that Taiwan is part of China. Although significant economic and cultural relations have been established between the Republic of China and the PRC, such as the engagement of the Economic Cooperation Framework Agreement, or ECFA, in 2010, relations may become strained again. The PRC government has refused to renounce the use of military force to gain control over Taiwan. Past developments in relations between the Republic of China and the PRC have on occasion depressed the market prices of the securities of companies in the Republic of China. Relations between the Republic of China and the PRC and other factors affecting military, political or economic conditions in Taiwan could materially and adversely affect our financial condition and results of operations, as well as the market price and the liquidity of our securities. In addition, the complexities of the relationship between the ROC and PRC require companies involved in cross-strait business operations to carefully monitor their actions and manage their relationships with both ROC and PRC governments. In the past, companies in the ROC, including us, have received minor sanctions such as travel restrictions or minor monetary fines by the ROC and/or PRC governments. We cannot assure you that we will be able to successfully manage our relationships with the ROC and PRC governments for our cross-strait business operations, which could have an adverse effect on our ability to expand our business and conduct cross-strait business operations.

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

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

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

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

Our actual financial results may differ materially from our published guidance.

Prior to 2013, we used to voluntarily publish our operating results guidance on an annual basis in accordance with ROC GAAP. Beginning in 2013, we plan to continue voluntarily publishing our operating results guidance on an annual basis in accordance with Taiwan IFRS. We may from time to time update our operating results guidance after evaluating the effects of any changes to the estimates and assumptions that we used to calculate our projections of our operating results. Our projections are based on a number of estimates and assumptions that are inherently subject to significant uncertainties and contingencies, including the risk factors described in this annual report. In particular, our projections are forward-looking statements that are necessarily speculative in nature, and it can be expected that one or more of the estimates on which the projections were based will not materialize or will vary significantly from actual results, and such variances will likely increase over time.

Our results of operations and financial condition upon the adoption of new financial reporting standards may differ materially from our reported results of operations and financial condition under ROC GAAP.

The Financial Supervisory Commission, or the FSC, in the ROC, supervises the financial and business matters of publicly-held companies, and we are required to comply with relevant regulations promulgated by the FSC. We have historically presented our consolidated financial statements, including our consolidated financial statements for the year ended December 31, 2012, in accordance with ROC GAAP for purposes of our filings with the TWSE, with reconciliation to U.S. GAAP for certain filings with the SEC. Effective January 1, 2013, companies listed on the TWSE, including us, must report their financial statements under Taiwan IFRS pursuant to the requirements of the Framework for Adoption of International Financial Reporting Standards by Companies in the ROC promulgated by the FSC on May 14, 2009. Accordingly, we have adopted Taiwan IFRS for reporting in the ROC our annual consolidated financial statements beginning in 2013 and our interim quarterly unaudited consolidated financial statements beginning in the first quarter of 2013. While we have adopted Taiwan IFRS for ROC reporting purposes, we plan to adopt International Financial Reporting Standards issued by the International Accounting Standards Board, or IFRS, which differs from Taiwan IFRS, for certain filings with the SEC, including our annual reports on Form 20-F for the year ending December 31, 2013 and thereafter and our interim quarterly unaudited consolidated financial statements beginning with the three months ended March 31, 2013. Following our adoption of IFRS issued by the International Accounting Standards Board for SEC filing purposes, we will no longer be required to reconcile our consolidated financial statements with U.S. GAAP.

Taiwan IFRS differs from IFRS in certain significant respects, including to the extent that any new or amended standards or interpretations applicable under IFRS may not be timely endorsed by the FSC. In addition, Taiwan IFRS and IFRS differ in certain significant respects from ROC GAAP. See Item 5. Operating and Financial Review and Prospects Our Financial Reporting Obligations Recent Accounting Pronouncements . Because of the differences in accounting treatments, the adoption of Taiwan IFRS and IFRS may result in material and adverse changes to our results of operations and financial condition in our reported financial statements for the year ending December 31, 2013 and financial statements going forward. Furthermore, the dividends for 2013 that are expected to be declared at our 2014 annual general stockholders meeting will be calculated based on Taiwan IFRS. It is difficult for us to evaluate the precise impact of the adoption of Taiwan IFRS and IFRS on our financial reporting generally, or on our financial statements for the year ending December 31, 2013 or the year ended December 31, 2012, because the FSC may issue new rules governing the adoption of Taiwan IFRS and as other laws and regulations may be amended with the adoption of Taiwan IFRS. In addition, under Taiwan IFRS and IFRS, we are required to present the opening balance sheet on the transition date of January 1, 2012 with adjusted opening balances prepared under Taiwan IFRS and IFRS. Consequently, our consolidated financial statements for the year ended December 31, 2012 to be included in our annual report for the year ending December 31, 2013 may differ materially from those included in this annual report, even though they relate to the same fiscal year. Similarly, the selected comparison financial information to be included in our quarterly earnings releases in 2013 may also differ materially from those released historically.

Risks Relating to Ownership of Our ADSs and Common Shares

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

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

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

Our common shares are traded on the Taiwan Stock Exchange, or TWSE, which has a smaller market capitalization and is more volatile than the securities markets in the United States and many European countries. The market value of our ADSs may fluctuate in response to the fluctuation of the trading price of our common shares on the TWSE. The TWSE has experienced substantial fluctuations in the prices and trading volumes of listed securities, and there are currently limits on the range of daily price movements. In recent years, the TWSE Index reached a peak of 10,202.20 in February 2000 and subsequently fell to a low of 3,446.26 in October 2001. During 2012, the TWSE Index peaked at 8,144.04 on March 2, 2012, and reached a low of 6,894.66 on June 4, 2012. On April 12, 2013, the TWSE Index closed at 7,821.63. The TWSE has experienced certain problems, including market manipulation, insider trading and payment defaults. The recurrence of these or similar problems could have a material adverse effect on the market price and liquidity of the securities of Taiwan companies, including our ADSs and common shares, in both the domestic and the international markets.

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

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

The laws of the Republic of China limit foreign ownership of our common shares. Prior to March 1, 2006, the Ministry of Transportation and Communications, as the competent authority under the Telecommunications Act, had the power to prescribe the limits on foreign ownership of our common shares. After the formation of the NCC on March 1, 2006, the NCC replaced the Ministry of Transportation and Communications as the competent authority under the Telecommunications Act pursuant to the National Communications commission Organization Law, or the Organization Law. The NCC and the Ministry of Transportation and Communications reached an agreement on foreign ownership of Chunghwa Telecom. An announcement issued by the Ministry of Transportation and Communications on December 28, 2007 stipulated that direct holdings by foreign investors in Chunghwa Telecom cannot exceed 49% of our outstanding share capital and the total direct and indirect holdings by foreign investors cannot exceed 55% of our outstanding share capital. As of April 12, 2013, foreign direct holdings of our outstanding share capital is at 14.87% . If we fail to comply with the applicable foreign ownership limitations, our licenses to operate some of our businesses could be revoked. Moreover, we cannot predict the manner in which the NCC will exercise its authority over us, or whether NCC will lower the foreign ownership cap at any time.

If we are deemed to be in violation of our foreign ownership limitations, any consequences arising from such violation may materially and adversely affect us. Moreover, since we are unable to control ownership of our common shares or ADSs representing our common shares, and because we have no ability to stop transfers among stockholders, or force particular stockholders to sell their shares, we may be subject to monetary fine or lose our licenses through no fault of our own. In that event, our business could be disrupted, our reputation could be damaged and the market price of our ADSs and common shares could decline. These limitations may also materially and adversely affect our ability to obtain adequate financing to fund our future capital requirements or to obtain strategic partners, and alternate forms of financing may not be available on terms favorable to us or at all.

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

The ability to deposit shares into our ADS program is restricted by Republic of China law, under which no person or entity, including you and us, may deposit our common shares into our ADS program unless the Securities and Futures Bureau has not objected within a prescribed period following the filing with it of an application to do so, except for the deposit of the common shares into our ADS program and for the issuance of additional ADSs in connection with:

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

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

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

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

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

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

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

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

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

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

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

- any cash dividends or distributions received from the common shares represented by ADSs.

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

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

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

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

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

ITEM 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

Our legal and commercial name is Chunghwa Telecom Co., Ltd. We were officially established on July 1, 1996 as part of the privatization efforts by the government of the Republic of China and operate under the Statute of Chunghwa Telecom Co., Ltd. Prior to our formation, we were operating as a business unit of the Directorate General of Telecommunications. The common shares of the Company have been listed on the TWSE under the number 2412 since October 2000 and its ADSs have been listed on the New York Stock Exchange under the symbol CHT since July 2003. In August 2005, we became a privatized company as the ownership by the government of the Republic of China was reduced to less than 50%. Today, we are the largest full telecommunication service provider in Taiwan. Our principal executive offices are located at 21-3 Hsinyi Road, Section 1, Taipei, Taiwan, Republic of China, and our telephone number is (886) 2-2344-5488. Our website address is *http://www.cht.com.tw*. The information on our website does not form a part of this annual report. Our agent for service of process in the United States is CT Corporation System, 111 Eighth Avenue, New York, NY 10011.

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

- domestic fixed communications services, including local and domestic long distance telephone services, broadband access services, local and domestic long distance leased line services, Wi-Fi services, MOD services, domestic data services and other domestic services;
- mobile communications services, including mobile services, sales of mobile handsets and data cards and other mobile services;
- internet services, including HiNet, our internet service, internet value-added services, data communication services, internet data center services, and other internet services;

- international fixed communications services, including international long distance telephone services, international leased line services, international data services, satellite services and other international services; and

- other services, including non-telecom services.

In addition to these traditional telecommunication services, we also focus on selected ICT services and advanced development, such as cloud computing.

For each of our key services, we enjoy leading positions across a number of areas in terms of both revenues and customers:

- we are Taiwan s largest fixed communications services provider as well as Taiwan s largest mobile communications service provider;

- we are Taiwan s largest broadband access provider; and

- we are Taiwan s largest internet service provider.

In 2012, our revenues under ROC GAAP were NT$220.1 billion (US$7.6 billion), our consolidated net income was NT$41.0 billion (US$1.4 billion) and our basic earnings per share was NT$5.14 (US$0.18).

In 2012, we made capital expenditures totaling NT$33.3 billion (US$1.1 billion), of which 59% was related to our domestic fixed communications business, 22% was related to our mobile communications business, 10% was related to our internet business, 7% was related to our international fixed communications business and 2% was related to our other businesses. See Item 5. Operating and Financial Review and Prospects B. Liquidity and Capital Resources Capital Expenditures for a discussion of our capital expenditures.

Competitive Strengths

We believe that we are well positioned to take advantage of the increasing opportunities in the telecommunications market in Taiwan as new technologies evolve. In particular, we have maintained our leading market share in mobile communications and internet services. Furthermore, we have enjoyed greater flexibility in making purchasing and other business decisions after we were privatized in August 2005.

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

We believe that our primary competitive strengths are:

- our broad customer base in Taiwan;

- our position as an integrated, full-service telecommunications provider in Taiwan; and

- our capital resources and technology, which we believe we can build on to expand our leading position in the mobile communications and internet services markets, including through our continued construction of our existing 3G/HSPA/ HSPA+/Dual cell HSPA+ mobile network, our expansion of FTTx broadband access services, IP-based MOD services, fixed-line/mobile value added and cloud computing related services, and our future construction of a fourth generation long-term evolution mobile network if we win the technology neutral spectrum license at the end of 2013.

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We have a broad customer base in Taiwan.

We are the largest telecommunications service provider in Taiwan with a broad customer base across all of our service offerings. Despite deregulation and an increase in competition in the Taiwanese telecommunications industry, we have maintained a market leading position in our primary service offerings of fixed communications, mobile communications and internet services. We believe our broad customer base in each of our service offerings grants us a distinct competitive advantage to maintain our existing customers and attract new customers and increases the chance of success for the launch and popularization of new products. As the telecommunications industry continues its trend of converging fixed communications, mobile communications and internet services, we believe that our comprehensive service offerings place us in a strong position to offer converged products and services to our customers.

We are an integrated full-service telecommunications provider in Taiwan.

We are the largest telecommunications service provider in Taiwan with a leading position in fixed communications services, mobile communications services and internet services.

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

Broad network coverage. The breadth of our network and our ownership of the last-mile infrastructure in Taiwan, which comprises the connection between the local telephone service provider s switching centers to the end-users buildings or homes, provides us with access to existing and potential customers and creates a platform for expanding our services. In order to provide higher bandwidth services for our customers, we have been constructing our FTTx network since 2003. We have successfully migrated many of our customers from lower-speed to higher-speed internet access services and upgraded ADSL subscribers to FTTx, which offers even higher speeds by using fiber optic technology. The number of our FTTx subscribers has exceeded that of our ADSL subscribers since 2011. As of December 31, 2012, network coverage of FTTx with speeds of 50 Mbps and 100 Mbps was approximately 81.9% and 73.6 %, respectively. In addition, our mobile communications network provides nationwide coverage. Our large cellular spectrum allocation together with our network of 19,941 base stations positions us well for the continued expansion of our mobile services in Taiwan. We are also continuing to build our Wi-Fi network to offload 3G capacity in residential areas and public areas where subscriber density and usage is high, such as urban areas, airports and convenience stores.

Brand awareness, distribution channels and customer service. Our principal brands Chunghwa Telecom, emome and HiNet have a reputation for quality and reliability. We serve our large and well-established customer base through our extensive customer service network in Taiwan, including 17 operations offices, 392 service centers, 238 exclusive service stores and 6 customer service call centers. We are continuing to expand and transform our retail stores while increasing the number of our service centers throughout Taiwan. We also offer comprehensive and high-quality point of sale and after sale services in our service centers, stores and over the internet. Our extensive sales and distribution channels help us attract additional customers and develop new business opportunities. In 2012, we also obtained several domestic and international awards which recognized our service quality, corporate governance and our fulfillment of corporate social responsibility. In the Reader s Digest Trusted Brands Awards, we have stood out and won the Platinum Award of Telecom Company in Taiwan for nine consecutive years since 2004. We were also awarded the Excellence in Corporate Social Responsibility Award by the Common Wealth Magazine, Excellent Service Award 2012 by Global Views, and were ranked A^+ in Transparency and Information Disclosure by the Taiwan Securities and Futures Institute.

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

Comprehensive customer billing infrastructure. As Taiwan s leading telecommunications services provider, we have extensive resources and infrastructure relating to billing services. We intend to continue taking advantage of this unique attribute by offering bill collection services to internet content providers and other entities that lack the necessary resources and infrastructure for effective customer billing.

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

Enhancing position in our leading markets. We expect our mobile value-added service, fixed broadband value-added and ICT services to continue to be the key drivers of our future growth. With our leading market share, we enjoy substantial economies of scale in equipment procurement as well as the marketing of our products and services.

Strong capital structure. We believe we have great financial resources in Taiwan. Our low debt-to-equity capital structure, together with our high levels of cash and operating cash flows, provides us with the flexibility and resources to invest in capital intensive and growing businesses. In particular, we continue to invest in broadband internet protocol networks, fiber-optic networks, and 3G/HSPA, HSPA+, Dual cell HSPA+ mobile communications networks and services. We have also begun to make investments in or to acquire other companies which provide complementary telecommunications and internet-related services to further expand our business and offer new products and services.

Advanced network technology. Since 2003, we have developed and upgraded our existing infrastructure for both mobile and fixed-line networks. We developed a high-speed internet protocol backbone network, expanded the coverage of our ADSL network, and deployed a 3G network. In 2008, we launched a long-term next generation network construction project that will upgrade our local fixed-line networks to high-speed packet-based digital networks with FTTx technologies, including FTTC/N, FTTB and FTTH, in order to provide high speed internet, VoIP, MOD and high definition television, or HDTV, services. We have also upgraded our 3G network to HSPA and HSPA+, and Dual cell HSPA+. In 2012, we expanded HSPA/HSPA+/Dual cell HSPA+ coverage to provide better mobile internet services. Our investment in network infrastructure places us in a position to capture a significant share of the internet and high-speed data transmission market.

Research and development expertise. As of March 31, 2013, we employ over 2,474 research professionals and engineers whose principal focus is to develop advanced network services and operations support systems and to build selected core technologies. In 2012, our research and development expenses accounted for 1.7% of our revenues under ROC GAAP. We believe our focus on research and development will allow us to efficiently develop and deploy new technologies and services ahead of our competitors.

Business Strategy

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

Our key strategic objectives are to maintain our position as a leading integrated telecommunications services provider in Taiwan and to enhance our leadership position in growing markets, such as the mobile services and internet services markets, including fixed-line and mobile broadband access services and value-added services. By leveraging on our solid and quality customer base, expanded network capacity and enhanced network capability, we plan to further enhance our fixed and mobile value-added services, or VAS, offerings and promotion. We have also introduced new ICT services as well as cloud computing services by leveraging enterprise high speed broadband demand to offer VAS and explore emerging service.

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

Focus on our core strengths while maintaining our market share

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

Fixed communications: Our strategy is to maintain our position as the market leader in domestic fixed communications. We aggressively introduced new technology and equipment of fixed network to improve operational efficiency and facilitate business transformation. In the meantime, we also provide MOD, cloud-based multi-screen services and internet of things services including Intelligent Energy Network, or iEN, street surveillance services to improve customers digital life. We expect that these initiatives will enhance customers loyalty and generate more revenues.

Broadband services: We strive to maintain our broadband market share. Therefore, we are continuing the build-out of our FTTx infrastructure. We expect that we will be able to offer broadband services with speeds of 100 Mbps to 85% of households in the ROC by the end of 2013, including coverage of FTTH reaching 50% of households in the ROC. As more customers within our current coverage area subscribe for 100 Mbps broadband services or FTTH services, we will still need to incur additional capital expenditures to deploy such services from the cross-connection boxes to each customer s premises. In addition, we plan to incur additional capital expenditures to further construct our FTTH infrastructure to expand our coverage area throughout the ROC. We believe these efforts will help us maintain our competitive advantage for broadband services. A high quality broadband network is also essential for our high-definition MOD services.

- We provide ADSL and FTTx services to 4.6 million customers, which represented more than 79.2% of Taiwan s fixed-line broadband customers by the end of 2012. Approximately 59.7% of our broadband customers were using FTTx services as of December 31, 2012.

- We typically realize higher average revenue per user for our FTTx internet services, and we continue to offer various incentives for our ADSL and other internet customers to upgrade to our FTTx services. In 2012, FTTx revenue reached 75.6% of our total broadband revenue.

Mobile Communications: We offer our mobile services via both 2G and 3G networks. For 3G, wideband code division multiple access, or WCDMA, is adopted. In order to meet the demand from our customers for high-speed mobile data access, we upgraded our 3G mobile service to High-Speed Packet Access, or HSPA technology on September 12, 2006 and to HSPA+ services in 2010. The prevalence of smart devices, such as smart phones and tablet PCs that utilize large amounts of mobile data, has become a challenging task for all mobile operators. We are continuing to develop Heterogeneous Network, or HetNet, to meet such demand. HetNet incorporates macrocells for large area coverage, and small cells including micro cells, pico cells, femtocells and Wi-Fi to increase our data capacity. Our strategy for mobile service includes the following initiatives:

- Further introducing mid- to low-tier smartphones to expand our mobile internet subscriber base;

- Promoting the migration of 2G customers to 3G network by offering various mobile handsets combined with attractive value-added services and product packages;

- Expanding our HSPA+/Dual cell HSPA+ coverage and enhancing the base station bandwidth to attract more mobile internet customers;

Constructing more Wi-Fi hotspots and hot zones to offer wireless internet access service and to offload 3G data traffic; in particular, we plan to construct over 45,000 Wi-Fi Hotspots and 200 hot zones in metropolitan areas by the end of 2013;

Enabling 3G/Wi-Fi auto-authentication to enhance customer experience;

Converging fixed communications and mobile communications services to provide customers with access to personalized information through personal computers or mobile handsets; and

Taking advantage of our superior brand and network quality to attract our competitors customers.

Internet services: Our strategy for internet services is to continue to build on the success of our HiNet internet services and enhance our internet value-added services.

We are developing new media to provide both higher-speed access as well as attractive content to our customers. We are also continually enhancing our internet value-added services, such as online games, internet music, internet banking and internet protocol video services, including hiChannel, an internet platform where customers can view videos and multimedia content.

Emerging services: Our emerging services include ICT, cloud computing and integrated services. We have been providing ICT services since 2009, including iEN, and Intelligent Transportation System, or ITS, services. Our experience with ICT services positions us well to develop and offer cloud computing services, and we anticipate that cloud computing services could become an important area of growth for telecom operators in the near future. We started to offer hicloud Compute as a Service, or CaaS and provide customers 24-hour installation services in 2010. We started to offer hicloud Mall in 2011, which allows Independent Software Vendors, or ISV to offer their application software in the hicloud Mall for sale. In 2012, we also introduced cloud-based multi-screen services, named Hami+ providing music, video, news, e-book, weather, traffic information, personal cloud and payment services. The integration of platform and network enables our customers to use and purchase the service through their PCs, IPTV, MOD, tablet PCs and smart phones, and satisfies users needs to utilize those services anytime, anywhere with any device. For enterprise customers, we introduced hicloud Virtual Private Cloud, or VPC to facilitate the establishment of the dedicated cloud data center for centralized control of computing resources, storage services, network services and information security total solutions. We also introduced the hicloud box to provide data storage and file sharing services, which helps enterprise customers reduce storage costs while providing a platform to share resources in a protected environment. In 2012, our laboratory independently developed an open source cloud operating system under the Virtuoso brand name and cooperated with Wiwynn Corporation to provide cost effective cloud appliances equipped with our open source cloud operating system. We are continuing to expand the scope and variety of our integrated services to create more value for our customers.

Emphasize quality of service and customer satisfaction

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

In order to ensure that our quality of service will translate into strong customer loyalty, we plan to continue to focus on and invest in the provision of a full range of services that emphasize customer care from the point of sale onward. For example, we have extended the focus of our corporate customer services from major accounts to include small and medium-sized enterprises and in January 2007 established our Enterprise Business Group. As of December 31, 2012, our Enterprise Business Group was staffed by 371 professionals and offered packaged and customized services, customer-oriented solutions and integrated information and communications services. We have completed the integration of our call centers, all of which can now be reached by calling a single number 123 . We offer 24-hour customer service, including the handling of service and billing inquiries with the assistance of an Interactive Voice Response, or IVR, system. To improve the quality of our customer services, we implemented a customer relationship management system, which encompasses, among other things, a customer complaint system, a business information database for the use of our call centers, and a data mining system to enhance our sales and market analysis efforts.

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Improve operational efficiency and cost structure

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

Capital expenditures. Our long-term goal is to optimize our capital expenditures by focusing on investing in innovative products and services with attractive return profiles. To catch up with the fast evolution of digital devices and network applications, we continue the construction of our fiber-based fixed-line and mobile network to increase the network bandwidth and enhance operational efficiencies. In particular, we plan to construct high capacity Wi-Fi/Fiber-Wireless networks to offload mobile network traffic and upgrade network equipment to improve operational efficiency and reduce operating cost. For example, we have focused on redesigning optical distribution networks, consolidating aggregate networks, simplifying network layers, centralizing network planning and equipment procurement, designing Single Radio Access Networks, developing remote automatic Operations, Administration, Maintenance and Provisioning systems and following precision construction policy to enhance equipment utilization rate and improve management efficiency.

Personnel costs. We seek to improve our operational efficiency by reducing our personnel costs. For example, we offered voluntary retirement programs once each year since 2005, which resulted in reductions of 6,148 employees in total as of December 31, 2012. We also hired more than 3,953 new employees after our privatization in August 2005. Since then, we continued to align our organizational structure by integrating various operating units and departments. We will also continue to reallocate our personnel from traditional fixed-line services to our growing businesses and to our marketing and customer services departments, as well as exploring outsourcing opportunities where we deem appropriate. On January 30, 2013, we set up a human resource company, Honghwa Human Resources Co., Ltd., in order to save on personnel expenses as well as to provide customers 24 hours a day, 7 days a week service installation and retail stores service.

Expand our business through alliances, acquisitions and investments

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

Alliances. We have formed and will continue to pursue alliances with information content providers, multimedia service platform providers, customer premises equipment providers, internet portal operators, and information and communication technology solutions partners to diversify our business operations and enhance our service offerings. In November 2012, we entered into a memorandum of understanding with Rhythm & Hues Studios, who has won the Academy Award for Best Special Effects twice and the Academy s Scientific & Technical Award four times. We expect this proposed alliance with Rhythm & Hues Studios to facilitate our ICT development. In January 2013, we signed a memorandum of understanding with Wiwynn Corporation. We aim to corporate with Wiwynn Corporation by combining its hardware solution with our cloud technology to jointly provide customers plug-and-play appliance and explore domestic and overseas computing business opportunities. See B. Business Overview Mobile Communications Business Mobile Services for a discussion of our alliance on mobile services.

Acquisitions and Investments. We have focused our acquisition strategy on making acquisitions of companies that we believe to be complementary to our long-term strategic goals. In addition, after our privatization, we have focused our investment strategy on the development of new businesses and the enhancement of our operation efficiency. Recently we have entered into the following notable transactions:

In 2010, we acquired a 6.67% equity interest in Innovation Works Limited, or IW. Our shareholding decreased to 1.92% in 2011 due to issuance of employee options. In June 2010, we invested 13.3% in Innovation Works Development Fund, or IWDF, which was established to support the development of Innovation Works Limited. After IWDF s US$180 million capital increase in 2011, our shareholding in IWDF decreased to 4.4%. We believe our investment in IW and IWDF, which mainly conduct business operations or invest in the mobile internet industry in mainland China, will help open up our business opportunities in e-commerce, mobile internet and cloud computing services in the mainland.

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In June 2010, we became a 18.2% stockholder of CQi Energy Infocom Inc., or CQi, which engages mainly in intelligent energy network management services.

In September 2010, we established Chunghwa Precision Test Tech. USA Corporation, that engages in the testing service of semi-conductor components and printed circuit boards.

In March 2011, we established a wholly owned subsidiary Chunghwa Telecom (China) Co., Ltd., which engages mainly in providing services of planning, design, and integration of information systems.

In May 2011, we established a wholly owned subsidiary Chunghwa Telecom Vietnam Co., Ltd. in Vietnam, which engages mainly in providing International Private Leased Circuit, or IPLC, and iEN, services to Taiwanese enterprises in Vietnam.

In May 2011, we, together with President Chain Store Corporation and EasyCard Corporation, established Dian Zuan Integrating Marketing Co., Ltd., or DZIM. As of December 31, 2012, we owned 33.34% of DZIM. DZIM engages mainly in information technology services and general advertising services.

In July 2011, we established Chunghwa Sochamp Technology Inc., which mainly engages in license plate recognition systems. As of December 31, 2012, we owned 51% of Chunghwa Sochamp Technology Inc.

In August 2011, we and United Daily News established a joint venture, Smartfun Digital Co., Ltd., which mainly engages in sales of educational software and providing digital parenting education. As of December 31, 2012, we owned 65% of Smartfun Digital Co., Ltd.

In September 2011, we invested in Huada Digital Corporation and owned 50% of this company as of December 31, 2012. Huada Digital Corporation mainly engages in providing software services.

In February 2012, we subscribed for shares of China Airlines Ltd. in an equity offering and became a 5.07% stockholder of China Airlines Ltd. We expect to leverage China Airlines Ltd. s expertise and operational experience within the tourism and transportation industries to develop relevant ICT services, including intelligent tourism and transportation cloud services. See Acquisitions and Investments for further information. We have developed a tourism cloud platform to provide travel information and products as well as physical and virtual channels to facilitate the operation of different parties in tourism industry. We expect to have 100,000 hits per month at the end of 2013.

In November 2012, we established Hua-Xiong Information Technology (China) Co., Ltd., which mainly engages in providing intelligent systems and energy saving systems and services for buildings. As of December 31, 2012, we owned 51% of Hua-Xiong Information Technology (China) Co., Ltd.

In January 2013, we set up a human resource company, Honghwa Human Resources Co., Ltd., in order to save on personnel expenses as well as to provide customers 24 hours a day, 7 days a week service installation service and retail stores service.

Please also see notes 1 and 13 to our consolidated financial statements included elsewhere in this annual report for our current strategic investments.

Going forward, we may consider making other equity investments and acquisitions that we believe are complementary to our business and strategic goals. Our future investment will be aimed at expanding our business scale and scope, making better use of our research and development resources and operational experience and increasing our revenues through investing in core telecom businesses as well as value-added services. We expect to target the markets of our overseas investments from Southeast Asia to China while carefully evaluating the risks involved.

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Maintain focus on maximizing stockholder value

We are committed to maximizing stockholder value and we intend to maintain our high dividend payout policy. Following our privatization, we have more flexibility to implement capital management initiatives, including possible repurchases of our outstanding common shares and increases in our leverage through debt financing. We bought back 121,075,000 common shares between August 29, 2007 and October 25, 2007 and cancelled those shares on December 29, 2007 and February 21, 2008, respectively.

We continued our capital reduction plan from 2007 to 2010. We effected the last capital reduction plan in 2010 by reducing 20% capital stock in the amount of NT$19.4 billion. The cash payment of NT$19.4 billion was made on January 25, 2011 to our stockholders.

B. Business Overview

Our Principal Lines of Business

Our core business segments are our domestic fixed communications business, mobile communications business, internet business and international fixed communications business.

Domestic Fixed Communications Business

The provision of domestic fixed communications services is one of our principal business activities. Our domestic fixed communications business includes local and domestic long distance telephone services, broadband access services, local and domestic long distance leased line services, multimedia on demand services, and domestic other services including ICT, corporate solution services, cloud computing services, etc. We are the largest provider of local and domestic long distance telephone services in Taiwan. We also provide interconnection with our fixed-line network to other mobile and fixed-line operators. Our revenues from domestic fixed communications services were NT$70.7 billion or 34.9% of our revenues in 2010, NT$79.4 billion or 36.5% of our revenues in 2011, and NT$75.5 billion (US$2,599.0 million) or 34.3% of our revenues in 2012. In general, we expect that revenues from our domestic fixed communications business as a percentage of our total revenues will continue to decline primarily due to (i) the expansion of our mobile communications services and (ii) the general trend of a continued decline in fixed-line voice traffic. However, in 2011, our domestic fixed communications business increased as a percentage of our total revenues due to the change in pricing and collections policies for fixed-line-to-mobile phone calls. Starting on January 1, 2011, the fixed-line operators now set and collect the tariffs for fixed-line-to-mobile phone calls, whereas prior to January 1, 2011, these functions were performed by the mobile operator. Please see Item 4. Information on the Company B. Business Overview Regulation Interconnection Arrangements . In 2012, the general trend returned, as our domestic fixed communications business declined as a percentage of our total revenues.

Local Telephone

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

	Year ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
		(in billions)		(in millions)
Local telephone revenues:				
Usage	10.0	21.0	20.1	691.9
Subscription	17.0	16.7	16.4	564.5
Interconnection	2.4	1.4	1.2	41.3
Pay telephone	0.5	0.4	0.4	13.8
Other	2.9	2.2	2.1	72.3
Total	32.3	41.7	40.2	1,383.8

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We provide local telephone services to approximately 11.79 million customers in Taiwan. Our fixed-line network reaches virtually all homes and businesses in Taiwan. Revenues from local telephone services comprised 15.9%, 19.2% and 18.3% of our total revenues in 2010, 2011 and 2012, respectively. Approximately 74.0 % of our local telephone customers as of December 31, 2012 were residential customers. We are currently the leader of the local telephone service market, with an average market share of approximately 96.9%, 95.3% and 95.0% in 2010, 2011 and 2012, respectively.

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

	As of December 31,		
	2010	2011	2012
	(in thousands, except percentages and per household data)		
Taiwan population [1]	23,162	23,225	23,316
Fixed-line customers:			
Residential	9,165	8,948	8,728
Business	3,142	3,133	3,061
Total	12,307	12,081	11,790
Growth rate (compared to the same period in the prior year)	(1.1)%	(1.8)%	(2.4)%
Penetration rate (as a percentage of the population)	53.1%	52.0%	50.6%
Lines in service per household	1.15	1.11	1.07

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

Demand for local customer lines has historically been driven by population growth. However, with the development of mobile technologies, this trend has been declining. The number of fixed-line customers decreased by 2.4% in 2012 compared to 2011. We attribute the decrease in fixed-line customers to a general industry-wide trend of migrating from fixed-line services to mobile and internet telephony services. In adherence to a ruling by the Supreme Administrative Court, starting from September 2011, we no longer require our ADSL service subscribers to apply for our fixed-line services. We also allow our existing ADSL subscribers to unsubscribe their fixed-line service. The foregoing factors also caused the decrease in our fixed-line customers.

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

	Year ended December 31,		
	2010	2011	2012
	(in millions, except percentages)		
Minutes from local calls [1][2]	13,671	15,569	14,368
Growth rate (compared to the same period in the prior year)	(6.4)%	13.9%	(7.7)%

(1) Includes minutes from local calls made on pay telephones. It also includes minutes from fixed-line-to-mobile calls due to the change in policy starting from 2011.

(2) Calls to our HiNet internet service, which are recorded as part of our internet services, are not included in our local call minutes or revenues.

Minutes from local calls increased in 2011 due to the inclusion of minutes from fixed-line-to-mobile calls in this category starting from 2011 as a result of the NCC s change in policy for collecting the tariffs of fixed-to-mobile phone calls by our fixed communications business. Minutes from local calls decreased in 2012 due to the impact of mobile substitution and increased use of VoIP.

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

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

	Year ended December 31,		
	2010	2011	2012
	NT$	NT$	NT$
Average local telephone usage fee (per minute)	0.74	1.36	1.41
Growth rate (compared to the same period in the prior year)	0.5%	83.8%	3.7%

Average per minute usage charges increased from approximately NT$0.74 per minute in 2010 to approximately NT$1.36 per minute in 2011 and further to approximately NT$1.41 per minute in 2012. The significant increase in average per minute usage charges in 2011 was mainly due to the change in policy for collecting the tariffs of fixed-to-mobile calls from mobile service providers to fixed communications service providers since January 1, 2011, which granted our fixed communications business the right to set and collect the tariffs for fixed-line-to-mobile phone calls. Average per minute usage charges increased 3.7% to NT$1.41 in 2012, and we attribute this increase to the fact that users with lower average tariffs switched to using VoIP telephony services to a greater extent than users with higher average tariffs. Part of our competitive strategy is to offer customers innovative products and services intended to both secure customer loyalty and enhance revenues. In particular, our value-added services are designed to increase our call revenues by increasing the number of calls our customers make and by receiving fees for usage of the value-added services. These services include call waiting, caller identification, call forwarding, three-party calls, ring back tone and voicemail.

Domestic Long Distance Telephone

We provide domestic long distance telephone services in Taiwan. Total revenues from domestic long distance telephone services were NT$6.6 billion representing 3.3% of our total revenues in 2010, NT$5.8 billion representing 2.7% of our total revenues in 2011, and NT$3.8 billion (US$0.1 billion) representing 1.7% of our total revenues in 2012. Our average market share in the domestic long distance market was approximately 76.1%, 74.1% and 75.4% in 2010, 2011 and 2012, respectively.

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

	Year ended December 31,		
	2010	2011	2012
	(in millions, except percentages)		
Domestic long distance telephone service usage (minutes)	3,415	3,202	3,354
Growth rate (compared to the same period in the prior year)	(6.4)%	(6.2)%	4.7%

Along with the mandatory tariff reduction for domestic long distance telephone services, the minutes of use increased in 2012. See Item 5. Operating and Financial Review and Prospects Overview Tariff adjustments . However, we expect the minutes of use for domestic long distance calls will continue to decline as a result of traffic migration to mobile services and increased use of VoIP.

The following table sets forth information with respect to the average domestic long distance telephone usage charge per minute, excluding operator trunk dialing, for the periods indicated.

	Year ended December 31,		
	2010	2011	2012
Average domestic long distance telephone usage fee (per minute)	NT$ 1.61	NT$ 1.53	NT$ 0.90
Growth rate (compared to the same period in the prior year)	(4.2)%	(5.0)%	(41.2)%

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All domestic long distance calls, regardless of the distance between the calling parties, have the same tariff. We reduced our peak hour domestic long distance rate in January 2012 from NT$0.032 per second to our current rate of NT$1.6 per three minutes. Our current domestic long distance rate for off-peak hours is NT$1.0 per three minutes. Our average domestic long distance usage charge per minute decreased 41.2% in 2012 due to a further mandatory tariff reduction from the NCC. For more details of the NCC s mandatory tariff reduction, please see Item 5. Operating and Financial Review and Prospects Overview Tariff adjustments .

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

Broadband (ADSL+ and FTTx) Access

We provide broadband internet access through connections based on ADSL and our FTTx technology. FTTx generally offers a faster access medium for our internet customers compared to ADSL by using fiber optic technology. We are continuing the build-out of our FTTx infrastructure. The majority of our FTTx deployments consist of fiber-to-the-node with some fiber-to-the-building deployments. The majority of the local loops still use copper wires, and we do not have any present plans to upgrade the local loops to fiber optic lines. Because we typically realize higher average revenue per user for our FTTx internet services, we are offering various incentives for our ADSL and other internet customers to switch to our FTTx services.

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

	Year ended December 31,		
	2010	2011	2012
	NT$	NT$	NT$
		(in billions)	
Broadband access (ADSL and FTTx)	20.3	20.4	19.2

We provide broadband access services to other internet service providers that do not have their own network infrastructure, and as a result, our broadband customers also include some customers that use only our broadband data access lines and choose another provider for internet service provider, or ISP, services. We began to provide our ADSL service in August 1999 and had approximately 1.8 million customers as of December 31, 2012. As of December 31, 2012, approximately 71.9%, or 1.32 million, of our ADSL customers were also our HiNet subscribers. As a result of increased migration to our higher-bandwidth FTTx services, the number of our ADSL customers continued to decline in 2012.

The number of our FTTx customers increased significantly in 2010, 2011 and 2012 as prices became more affordable, coverage areas expanded and customer demand for higher bandwidth heightened. Many of new FTTx customers have migrated from using our ADSL internet services. We also provide FTTx access services to other internet service providers that do not have their own network infrastructure, and as a result, our FTTx customers also include some customers who only use us for the FTTx data access lines and choose another ISP to provide internet services. Of the approximately 2.72 million FTTx customers as of December 31, 2012, approximately 2.45 million were also our HiNet subscribers. We currently offer various promotional packages to encourage more migration of our ADSL subscribers to our FTTx service. As of December 31, 2012, 65.0% of HiNet subscribers accessed the internet through our FTTx service, and we expect this ratio to increase in the future as a result of these promotional measures.

Our market share of Taiwan s broadband market was approximately 80.5%, 79.2% and 79.2% in 2010, 2011 and 2012, respectively.

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The following table sets forth our broadband service customers as of each of the dates indicated.

	As of December 31,		
	2010	2011	2012
ADSL service customers (in thousands)	2,329	2,101	1,839
FTTx service customers (in thousands)	2,045	2,398	2,719
Average downlink speed (Mbps)	6.1	11.2	16.3

Our ADSL service offers downlink speeds that range from 1 Mbps to 8 Mbps and uplink speeds that range from 64 kilobits per second, or Kbps, to 640 Kbps. Our FTTx service offers downlink speeds of 12, 20, 50 and 100 Mbps matched with uplink speeds of 4, 5, 10 and 20 Mbps, respectively. As of December 31, 2012, approximately 88.7% of our customers had subscribed for downlink speeds of over 12 Mbps, and our average downlink speed was 16.3 Mbps.

We have experienced competition in the ADSL and FTTx service market from cable operators and other fixed-line operators. Our strategy is to continue the migration of ADSL subscribers to FTTx so as to increase the average revenue per user. In addition, in order to strengthen customer loyalty, we have provided free speed upgrades for ADSL customers who were using lower speed services since August 2010. In June 2011, we further reduced our broadband tariff, especially for higher speed services such as 20 Mbps and 50 Mbps, in order to speed up the migration to fiber solutions and facilitate the take-up of relevant applications. Although the lower broadband tariff had a temporary impact on our revenue, we believe the speed upgrade will have a positive effect on our promotion of broadband value-added services in the long run.

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

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

	Year ended December 31,		
	2010	2011	2012
	NT$	NT$	NT$
Average revenue per user for HiNet dial-up services per month(1)	17	16	15
Average revenue per user for ADSL services per month(2)	598	569	437
Average revenue per user for FTTx services per month(3)	1,019	945	896

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

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

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

The decline of our ADSL average revenue per user over the last three years was due to the NCC s mandatory tariff reduction and our voluntary tariff reduction by 20% in the beginning of 2012. The decline of FTTx average revenue per user was due to the promotional packages and discounts provided for existing customers. For more details of the NCC s mandatory tariff reduction, please see Item 5. Operating and Financial Review and Prospects Overview Tariff adjustments .

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Leased Line Services Local and Domestic Long Distance

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

We provide data transmission services to major corporate customers in Taiwan. We also provide leased lines to other mobile and fixed-line service operators for interconnection with our fixed-line network and for connection within their networks.

The following table shows the bandwidth of local and domestic long distance lines leased to third parties as of each of the dates indicated.

	As of December 31,		
	2010	2011	2012
	(in gigabits per second, or Gbps)		
Total bandwidth	1,486.4	1,705.7	1,294.6

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

We continue to experience a decline in rental fees for all of our leased line products. We attribute the general decline in rental fees since 2000 to a general migration toward broadband services and increased competition from other service providers constructing their own lines. In response, we continue to implement marketing and service campaigns to retain our high-value corporate customers for our leased line products. Our local and domestic long distance leased line services revenues were NT$6.1 billion, NT$5.7 billion and NT$5.4 billion (US$0.2 billion) in 2010, 2011 and 2012, respectively.

Wi-Fi Services

We launched our wireless local area network service in May 2002. As of December 31, 2012, we had a total of approximately 1,280,315 residential and business customers that leased our access points. In addition, we had established 35,000 hot spots and 100 hot zones in public areas by the end of 2012, such as convenience stores, airports and international convention centers, where our smartphone subscribers can access our Wi-Fi network and help to offload 3G data network traffic.

Multimedia on Demand Services

Using video streaming technology through a set top box that connects to our FTTx and ADSL data connections, our customers can access TV programs, video-on-demand and other services. We had over 160 broadcasting channels and over 12,000 hours worth of on-demand programs and served approximately 1.2 million customers as of December 31, 2012. In addition, our video-on-demand service provides movies, dramas, animations, documentaries, e-learning and music programs for home entertainment. Also, as of December 31, 2012, we offered 69 high definition, or HD, channels and other HD video-on-demand programming, such as sports, movies and knowledge materials. Starting from the fourth quarter of 2012, we cooperated with Hon Hai Precision Industry Co., Ltd., or Hon Hai, to co-sell its sixty inches TV sets with our IPTV service by bundling the two products together, which provides customers high-quality HD user experience. This effort is expected to further increase customer loyalty and attract quality customers, who are increasingly demanding more high-quality entertainment options. Since this business model has proved to be successful, we will continue to cooperate with Hon Hai and other local TV manufacturers to co-market various sizes of TV sets with our quality MOD services. MOD revenues accounted for NT$1.1 billion, NT$1.4 billion and NT$2.0 billion (US$68.9 million) in 2010, 2011 and 2012, respectively.

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Other Domestic Services

Our other domestic services include information and communication technology services, cloud computing, corporate solution and bill handling services.

Mobile Communications Business

Mobile communications services are one of our principal business activities. Our mobile communications services include mobile services, sales of mobile handsets and data cards and mobile other services.

Mobile Services

We are Taiwan s largest provider of mobile services in terms of both revenues and customers. In 2010, we generated revenues of NT$73.1 billion, or 36.1% of our total revenues, from mobile services. In 2011, we generated revenues of NT$70.9 billion, or 32.6% of our total revenues, from mobile services. In 2012, we generated revenues of NT$72.5 billion (US$2,492.2 million), or 32.9% of our total revenues, from mobile services. The decrease of mobile services revenues in 2011 was primarily due to the NCC s change in policy for collecting the tariffs for fixed-to-mobile calls from mobile service providers to fixed communications service providers since January 1, 2011. As a result, our fixed communications business now has the right to set and collect the tariffs for fixed-line-to-mobile phone calls. However, the interconnection and transition fees paid by our fixed communication business and received by our mobile segment is deemed as internal revenue and not recognized as external revenue of our mobile segment, while the aforementioned fees received by the alternative mobile operators were recognized as external revenue. In 2012, we managed to increase our mobile revenue by promoting mobile internet services, which fully offset the decline of mobile voice revenue due to the NCC s mandatory tariff reduction and market competition.

	Year ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
		(in billions)		(in millions)
Mobile services revenues:				
Usage[(1)]	53.0	45.6	42.1	1,449.2
Interconnection	7.2	7.5	7.3	251.3
Mobile data	11.1	15.2	20.4	702.2
Other	1.8	2.6	2.7	92.9
Total mobile services	73.1	70.9	72.5	2,495.6

(1) Includes monthly fees.

As the market for mobile services has continued to expand, we have experienced growth in our mobile customer base. We are the largest mobile operator in Taiwan in terms of revenues and number of customers. We had 10.3 million mobile customers, for a market share of approximately 34.9% of total mobile customers and approximately 33.0% of total mobile services revenues in Taiwan, as of December 31, 2012.

In February 2002, the Ministry of Transportation and Communications granted 3G mobile services concessions to five companies, including us. In March 2002, we paid NT$10.2 billion to the government for our concession. Our 3G mobile services license is valid until December 31, 2018. In July 2005, we launched our 3G mobile services, using WCDMA technology. We have been allocated 15 MHz paired spectrum plus 5 MHz unpaired spectrum in the 2 GHz frequency band for 3G mobile services, and 15 MHz in the 900 MHz frequency band and 11.25 MHz in the 1800 MHz frequency band for GSM services and general packet-switched radio services, or GPRS. We offer the largest international roaming network among Taiwan mobile service providers. By the end of 2012, our 3G roaming contracts includes 175 networks in 80 countries, our 2G GSM roaming contracts include 379 networks in 190 countries, and our 2.5G GPRS roaming contracts include 301 networks in 139 countries.

As of December 31, 2012, we had 19,941 cellular base stations, including both GSM base stations and 3G cellular base stations, covering substantially all of Taiwan s population. We use these base stations to support both our GSM network and 3G networks. As of December 31, 2012, we had upgraded 10,384 3G cellular base stations with HSDPA capacity, and 2,400 GSM base stations with EDGE capacity in the larger metropolises of Taiwan. We will continue this process of implementing HSDPA and EDGE upgrades in the major areas of Taiwan.

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

	As of or for the year ended December 31,		
	2010	2011	2012
Taiwan population (in thousands)(1)	23,162	23,225	23,316
Total mobile customers in Taiwan (in thousands)(2)	27,840	28,862	29,449
Penetration (as a percentage of the population)(2)	120.2%	124.3%	126.2%
Total mobile revenues in Taiwan (in billions)(3)	NT$ 213.2	NT$ 217.0	NT$ 219.2
Number of our mobile customers (in thousands)(2)(4)	9,679	10,072	10,269
Our market share by customers	34.8%	34.9%	34.9%
Our market share by revenues	34.2%	32.6%	33.0%
Number of our prepaid customers (in thousands)(4)	945	1,052	1,124
Our prepaid customers as a percentage of our total customers	9.8%	10.4%	10.9%
Annualized churn rate(5)	10.35%	11.52%	13.26%
Minutes of use (in millions of minutes)			
Incoming	11,063	11,368	12,536
Outgoing	10,190	10,897	12,258
Average minutes of use per user per month(2)(6)	187	188	203
Average revenue per user per month(2)(7)	NT$ 643	NT$ 598	NT$ 594

(1) Data from the Department of Population, Ministry of the Interior, Republic of China
(2) The number of mobile customers is based on the number of subscriber identification module, or SIM, cards. Since 2006, the total number of mobile customers in Taiwan included 2G, 3G and personal handy-phone system, or PHS, customers.
(3) Data from the statistical monthly release by the National Communications Commission in the Republic of China, which include mobile revenues 2G, 3G and PHS.
(4) Includes GSM, GPRS and 3G services.
(5) Measures the rate of customer disconnections from mobile service, determined by dividing (a) our aggregate voluntary and involuntary deactivations (excluding deactivations due to customers switching from one of our mobile services to another) during the relevant period by (b) the average number of customers during the period (calculated by averaging the number of customers at the beginning of the period and the end of the period), and multiplying the result by the fraction where (c) the numerator is 12 and (d) the denominator is the number of months in that period.
(6) Average minutes of use per user per month is calculated by dividing the total minutes of use during the period by the average of the number of our mobile customers on the first and last days of the period and dividing the result by the number of months in the relevant period.
(7) Average revenue per user per month is calculated by dividing our aggregate mobile services revenues during the relevant period by the average of the number of our mobile customers on the first and last days of the period and dividing the result by the number of months in the relevant period.

Total mobile customers in Taiwan had reached approximately 29 million as of December 31, 2012. Mobile penetration was approximately 126.2% on the same date. The overall mobile services market experienced a slight increase of 1.01% in revenues in 2012 mainly due to the growth in mobile data service as a result of our smart phone promotions.

We began offering prepaid card services in October 2000 and prepaid 3G card services in February 2008. As of December 31, 2012, we had approximately 1.1 million prepaid customers, representing approximately 10.9% of our total mobile customers. Prepaid customers do not pay monthly fees but pay a higher usage charge on a per second basis. Once the prepayment has been fully utilized, a prepaid customer can make additional prepayments to continue the service. Alternatively, the customer may convert to become a post-paid customer while retaining the same telephone number.

We offer incentives, such as mobile handset subsidies, when new customers agree to sign a service contract with us or when existing customers renew their contracts with us ranging from 12 months to 30 months. We generally offer subsidies on mobile handsets equipped with more advanced data functions to promote the expansion of our 3G mobile services. Smart phones accounted for 69% of the total handsets we offered in 2012, and we expect the percentage to reach more than 75% in 2013. We expect our average subsidy per handset in 2013 to decrease as we focus more on promoting mid-tier and low-tier smart phones. At the same time, we expect to maintain our mobile internet market leadership.

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Our tariffs for post-paid mobile customers primarily consist of usage fees and monthly fees. When our customers are outside Taiwan, they pay roaming charges plus international long distance charges and, where applicable, local charges in roaming destinations. We negotiated with Vodafone, the largest telecommunications service provider in Europe, in November 2009 to join their global telecommunications alliance. As a result, we began offering our customers discounts on their roaming charges starting December 1, 2009. However, we expect our strategic alliance with Vodafone to be terminated by the end of April 2013 after our current agreement expires, as Vodafone has already entered into another strategic alliance with one of our competitors. We are negotiating with other providers for strategic cooperation for our roaming business, and we will continue cooperating with local operators in different countries. We also offer discounts on usage fees for calls made between our mobile customers to encourage subscription to our mobile service. Our 3G service provides a monthly flat rate service to our customers using our 3G service for internet purposes.

Our average revenue per user per month decreased from NT$598 in 2011 to NT$594 in 2012, mainly due to the NCC s mandatory tariff reduction. The strong promotion of our mobile internet services leads to the rapid growth in value-added service revenues and helps to cover for the decline in mobile voice revenues. In order to alleviate the impact of the decline in average revenue per user, we intend to continue introducing new value-added services and promote our 3G and wireless internet services.

In addition to our basic mobile services, we also offer a broad range of value-added telecommunications and information services. In August 2001, we introduced a platform of integrated mobile value-added services under the brand name emome . Our emome services offer a broad range of value-added services, including financial information, transaction services, emergency services access numbers, directory information, time, weather and traffic reports. In addition, we launched other mobile value-added services, such as JAVA games, unstructured supplementary service data, mobile internet and multimedia messaging services. After the launch of our 3G mobile services, we began providing video phone, video-on-demand and other related 3G mobile value-added services as well. In 2009, we successfully created a business model integrating smart phones with customer-tailored services, promoted our mobile internet service business, created the Hami value-added service platform and led the industry in providing e-book service and Hami Apps service. In addition to creating additional sources of revenues, we believe these services enhance customer loyalty and satisfaction and increase mobile traffic. Revenues from mobile data services represented 15.1%, 21.5% and 28.2% of our total mobile services revenues in 2010, 2011 and 2012, respectively.

Paging Services

Due to substitution by mobile services and a decline in demand for our paging services in recent years, beginning in February 2007, we started downsizing our paging services by limiting access to certain telephone prefixes. We ceased providing paging services in September 2011 as approved by the NCC.

Sales of Mobile Handsets

We engage in the distribution and sales of mobile handsets for use on our mobile network to customers through our directly-owned stores, our subsidiary, Senao International Co., Ltd., or Senao, and also through third-party retailers. See Marketing Strategy Distribution Channels and Sales and Distribution in Marketing, Sales and Distribution .

In January 2007, we acquired 31.33% equity ownership of Senao, a major distributor of mobile handsets in Taiwan. Senao has been listed on the TWSE under the number 2450 since May 2001. We obtained majority board representation in April 2007 through support from the largest beneficial shareholder, upon which it became a consolidated subsidiary of ours. At the general annual stockholder meeting of Senao in June 2010, we continued to maintain control of a majority of the board of directors through the continued support of the largest beneficial shareholder. Our equity ownership in Senao decreased from 31.33% as of January 15, 2007 to 28.24% as of March 31, 2013 due to the exercise of options by employees that were previously granted before 2007. Please refer to note 1 of our consolidated financial statements included elsewhere in this annual report for description about the control relationship between the parent company and Senao. Our investment in Senao enhanced our mobile handset distribution and sales capabilities. See Item 7. Major Stockholders and Related Party Transactions B. Related Party Transactions for a discussion of the agreement between the parent company and Senao about our business cooperation.

Other Mobile Services

Our mobile other services include information and communication technology services, corporate solution and bill handling services.

Internet Business

Our internet business includes HiNet, our internet service provider, internet value-added services, or VAS, data communication services, internet data center services, and other internet services. Our internet revenues represented 12.1%, 11.4% and 11.2% of our revenues in 2010, 2011 and 2012, respectively.

HiNet Internet Service

We are the largest ISP in Taiwan, with a market share of 69.6% as of December 31, 2012. As of December 31, 2012, HiNet had approximately 4.2 million subscribers. Our HiNet internet service generated revenues of NT$18.2 billion, NT$18.0 billion, and NT$17.0 billion (US$0.6 billion) in 2010, 2011 and 2012, respectively. Although our ISP service subscribers increased from 2010 to 2012, the revenues decreased mainly due to the tariff reductions for the HiNet ISP service and broadband access.

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

	As of December 31, (in thousands, except percentages)		
	2010	2011	2012
Total internet subscribers in Taiwan	5,888	6,092	6,101
HiNet subscribers:			
HiNet dial-up subscribers	507	487	469
HiNet ADSL subscribers	1,768	1,559	1,321
HiNet FTTx subscribers	1,818	2,132	2,451
Other access technology subscribers	3	4	3
Total HiNet subscribers	4,096	4,182	4,244
Market share[(1)]	69.6%	68.6%	69.6%

(1) Based on data provided by the National Communications Commission.

We have maintained our leading market position despite a highly competitive market with over 205 ISPs in Taiwan. We expect the competitive conditions currently prevailing in the internet service provider market to continue to intensify.

Internet Value-added Services

Our HiNet portal at www.hinet.net provides value-added services to our customers, such as network security, Blog, travel, games, e-learning, financial information, music, video, anti-virus and links to other portals. We charge fees for some of these services. We also receive commissions for transactions completed on some of these other portals. Our internet video portal at www.hichannel.hinet.net offers online entertainment services through the internet. In particular, our HiNet broadband (ADSL and FTTx) subscribers can access music, television programs, movies and other multimedia content on demand. We charge access fees for some of this content. We expect the revenues generated from these value-added services to grow as a percentage of our total internet services revenues.

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Data Communication Services and Internet Data Center Services

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

Internet data centers are facilities providing the physical environment necessary to keep computer network servers running at all times. These facilities are custom-designed with high-volume air conditioning temperature control systems, secure access, reliable electricity supply and connections to high-bandwidth internet networks. Data centers house, protect and maintain network server computers that store and deliver internet and other network content, such as web pages, applications and data. We currently have the greatest number of internet data centers in Taiwan compared to our competitors in Taiwan. We offer co-location, web hosting and application service provider services.

Other Internet Services

Our other internet services include government services, corporate solution and ICT services.

International Fixed Communications Business

Our international fixed communications business include international long distance telephone services, international leased line services, international data services, satellite services and international other services.

International Long Distance Telephone

We provide international long distance telephone services in Taiwan. Total revenues from international long distance telephone services comprised 6.4%, 5.7% and 5.5% of our revenues in 2010, 2011 and 2012, respectively. In addition, we provide wholesale international long distance services to international simple resale operators that do not possess their own telephone network or infrastructure.

Since international fixed communication services have been open for competition since 2001, we expect competition in this line of business will continue to intensify. Our average market share of the international long distance market was approximately 58.4%, 54.9% and 51.0% in 2010, 2011 and 2012, respectively. Our market share decreased in 2012 primarily because of the intense competition in the international telecommunications business from VoIP-based international long distance service providers and other international long distance service providers. Our international long distance services consist primarily of international direct dial services.

We commenced the wholesale of international long distance minutes to licensed international resale operators and other international carriers in 2001. International resale operators require a fixed-line operator in Taiwan to complete their long distance telephone services originating in Taiwan. In addition, other international carriers often find it less expensive to route international calls through Taiwan. These resale operators and carriers purchase from us large numbers of minutes at discounted rates. In 2010, 2011 and 2012, we sold 1,360 million, 1,206 million and 1,064 million of wholesale outgoing minutes, which represented approximately 50.1%, 47.1% and 42.2% of our total outgoing international long distance minutes, respectively. Revenues from the wholesale of international long distance minutes increased by 3.2% from NT$2,836 million in 2010 to NT$2,927 million in 2011, and decreased 0.48% to NT$2,913 million in 2012. We primarily attributed the decrease in the growth rate to intensified market competition.

International calls to our top five destinations represented 63.0% of our outgoing international long distance call traffic in 2012. International calls from our top five destinations represented 42.0% of our incoming international long distance call traffic in 2012.

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The following table shows the percentage of total outgoing international long distance minutes for our top five outgoing destinations in 2012.

Destination	Percentage of total outgoing minutes
Mainland China	29.9%
Indonesia	13.6
Philippines	7.9
Vietnam	7.2
Japan	4.4
Total of top five destinations	63.0%

The following table shows the percentage of total incoming international long distance minutes for our top five incoming destinations in 2012.

Destination	Percentage of total incoming minutes
United States	11.3%
Mainland China	10.9
Hong Kong	7.6
Indonesia	6.2
Malaysia	6.0
Total of top five destinations	42.0%

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

	As of December 31,		
	2010	2011	2012
	(in thousands, except percentages and incoming/outgoing ratio)		
Incoming minutes	1,915	1,737	1,529
Growth rate (compared to the same period in the prior year)	2.7%	(9.3)%	(11.9)%
Outgoing minutes	2,715	2,560	2,523
Growth rate (compared to the same period in the prior year)	7.4%	(5.7)%	(1.4)%
Total minutes	4,630	4,297	4,052
Incoming/outgoing ratio	0.71	0.68	0.61

Total outgoing international long distance minutes decreased 5.7% from 2010 to 2011 primarily due to an increase in our international long distance wholesale and transit businesses. Our outgoing call volume decreased by 1.4% from 2011 to 2012 primarily due to intensified market competition from VoIP-based international long distance service providers and other international long distance service providers. Our incoming call volume decreased by 9.3% from 2010 to 2011, and further decreased by 11.9% from 2011 to 2012 primarily due to the competition mentioned above.

Outgoing calls made by customers in Taiwan and by customers from foreign destinations using Taiwan direct service are billed in accordance with our international long distance rate schedule for the destination called.

Rates vary depending on the time of day at which a call is placed. Customers are billed on a six-second unit basis for international direct dial services.

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

	Year Ended December 31,		
	2010	**2011**	**2012**
Average international long distance usage charge (per minute)	NT$ 3.4	NT$ 3.6	NT$ 3.4
Growth rate (compared to the same period in the prior year)	(3.9)%	3.8%	(5.6)%

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The average charge per minute increased in 2011 compared with that in 2010 because we ceased to offer aggressive discounts and the decrease in the international long distance revenues was relatively smaller than the decrease in the number of minutes. In 2012, since other operators offered competitive tariff to grab market share, we reduced our retail price to maintain competitiveness which resulted in the lower average charge per minute.

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

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

	Year Ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
		(in billions)		(in millions)
Gross international settlement receipts	3.2	2.8	3.0	103.6
Gross international settlement payments	4.2	5.1	5.6	191.7

Our payments to international carriers on an aggregate basis have been greater than our receipts from these carriers primarily because our customers outgoing minutes exceeded incoming minutes. Both international settlement receipts and payments increased in 2012 because we promoted our international wholesale business.

In order to compete more effectively in the international long distance market, we have implemented innovative and customized discount calling plans and marketing campaigns directed at high-usage business customers. We also continue to promote our intelligent network services, including international VPNs, international toll free calling and calling card services, and our international long distance minutes wholesale business. Our subsidiary, Chief Telecom, launched its 070 phone-to-phone VoIP service in April 2009. In addition to the change in policy for collecting the tariffs for fixed-line-to-mobile calls starting from 2011, we are also required to pay transition fees to the mobile operators, which as a whole caused a negative impact on our revenues. As we did not have the right to set and collect the tariffs for our 070 service at that time, we filed with NCC to return 30 thousand 070 numbers assigned by the NCC to Chunghwa Telecom, until the NCC gives us the right to set and collect the tariffs for outbound calls from 070 numbers. The application was approved by the NCC on July 1, 2011.

Leased Line Services International

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

We provide data transmission services to major corporate customers in Taiwan. Since August 2001, licenses have been awarded to four undersea cable operators to engage in leased line services. Demand for high-speed data transmission services has been growing rapidly, as a result of growing consumer demand and lower tariffs due to increased competition. In particular, the total bandwidth of our lines leased increased by 118% in 2012.

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

	As of December 31,		
	2010	2011	2012
	(in gigabits per second, or Gbps)		
Total bandwidth	113.4	243.9	531.7

Rental fees for international long distance leased lines are generally based on transmission speed and distance.

We continue to experience a decline in rental fees for all of our leased line products. The decline in rental fees since 2000 has been substantial, particularly for international leased lines, partly as a result of competition from new international leased line service providers. In response, we continue to implement marketing and service campaigns to retain our high-value corporate customers. Our international leased line services revenues were NT$1.0 billion, NT$1.0 billion and NT$1.2 billion (US$41.3 million) in 2010, 2011 and 2012, respectively.

International Data Services

Our international data services include international IP VPN services and Taiwan internet gateway services. Total revenues for international data services were NT$1.0 billion, NT$1.1 billion, and NT$1.3 billion (US$44.8 million) for 2010, 2011 and 2012, respectively. Due to growth of the international corporations in Taiwan, we expect demand for IP VPN and Taiwan internet gateway services to continue to increase and our revenues from our international data services to continue to grow.

Satellite Services

We entered into a contract with ST-2 Satellite Ventures Pte., Ltd. on March 12, 2010 to lease capacity on the ST-2 satellite. The lease term is 15 years starting from the official start of operations of the ST-2 satellite, and the total contract value is approximately NT$6.0 billion. This contract requires a prepayment of NT $3.1 billion, and the remaining amount will be paid annually when ST-2 satellite starts its official operation. The ST-2 telecommunications satellite launched on May 21, 2011 and began commercial operation in August 2011. Please refer to note 28 of our consolidated financial statements included elsewhere in this annual report for further details.

In addition, we have two satellite communication centers that enable us to provide satellite value-added services and backup systems for use in major emergencies. We also provide satellite services to Southeast Asia.

Other International Services

Our other international services include corporate solution services.

Others

Our other business segments include our non-telecom services, including property sales made by our subsidiary, Light Era Development Co., Ltd.

Interconnection

We provide interconnection of our fixed-line network and mobile network with other operators.

The following table sets forth our interconnection revenues and costs for the periods indicated. These revenues and costs are included, depending on the nature of the call made, in domestic fixed communications or mobile communications revenues and expenses, respectively.

	Year Ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
		(in billions)		(in millions)
Interconnection revenues:				
Fixed-line (1)	2.7	1.6	1.3	44.8
Mobile (2)	7.9	8.3	8.0	275.4

	Year Ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
		(in billions)		(in millions)
Interconnection costs:				
Fixed-line (1)(3)	0.2	5.9	5.7	196.2
Mobile	7.4	8.4	7.7	265.1

(1) Includes local and domestic long distance telephone services.
(2) Includes SMS air time charges.
(3) The interconnection costs increased in 2011 due to the change in the policy for collecting the tariffs for fixed-line-to-mobile calls starting from 2011, and decreased in 2012 due to the decrease in the traffic of fixed-line-to-mobile calls.

Tariffs for telephone calls between our fixed-line customers and mobile customers of other mobile operators were set by the mobile operators before January 1, 2011. The mobile operators pay us interconnection fees based on minutes of use, regardless of who initiated the call. However, the NCC announced a change on August 4, 2010 that from January 1, 2011 onwards, the fixed-line network that initiated the call has the right to set and collect the tariffs for these fixed-line-to-mobile calls. Since we are the market leader of the local call services, in addition to the interconnection fees, we are also required to pay transition fees to the mobile operators for a period of six years. The transition fees will decrease gradually over the period and we will stop paying for them in 2017.The foregoing reasons caused the increase in our interconnection costs in 2011. In 2012, both interconnection revenues and costs decreased due to the decrease in both incoming and outgoing minutes.

The interconnection rate for calls initiated by mobile customers to fixed-line customers is NT$0.5219 per minute during peak times and NT$0.2718 per minute during off-peak times. The interconnection rate between fixed-line customers and other fixed-line customers is NT$0.32 per minute during peak times and NT$0.09 per minute during off-peak times. The interconnection rate for fixed-line customers to domestic or international long distance is NT$0.32 per minute. Additionally, the NCC has mandated mobile interconnection rate reduction over a period of four years starting on January 5, 2013. The rate should be reduced from NT$2.15 per minute to NT$1.15 per minute in four years with a CAGR of -14.5% .

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

Emerging Services

Our ICT services includes integrated services such as our Intelligent Energy Network, or iEN, and our Intelligent Transportation System, or ITS, services. Our iEN service helps companies and corporations implement energy saving measures through computer analysis of data. Our ITS service provides navigation, real-time traffic information and infotainment through mobile devices for cars and drivers. In addition to developing ICT businesses, such as iEN, ITS, IS, Call Center, IDC, we also pursue and bid for government projects aiming to boost economic development. In 2012, we won the bids for several government projects, such as New Taipei City Police Department Digital Video Surveillance System and TWSE Corporation Second Data Center .

Cloud Computing is also one of our key new business initiatives, as it is expected to be one of the main long-term growth platforms for telecom operators in the coming years. We have made advances in this segment throughout 2012 which we believe will position us as an industry leader over the long run. We continue to cooperate with the government network communication entities and independent software vendors to promote innovative cloud services and applications. We have already begun to offer Software as a Service Customer relationship management, or SaaS CRM, hicloud CaaS, and hicloud Apps mall to small and medium sized enterprises and public users. We have also made over 700 SaaS in hicloud Apps mall, and the number of our cloud customers exceeded 2,000 small and medium sized enterprises as of the December 31, 2012. Underpinning the rollout of our cloud computing services is our capability and experience in offering data center services to enterprise customers, including our ongoing initiative to build the largest cloud computing data center in Taiwan in anticipation of growing demand for this service. In 2012, we won the bids for some government projects, such as The Third Generation Motor Vehicle & Driver Information System, The Cloud Data Center of the Executive Yuan and Subordinate Commission and National Fire Agency The Cloud Plan of Disaster Prevention and Mitigation The Establishment of Infrastructure Service Platform, Operational Management and Message Service Platform . We believe the strength and reliability of our technology and services provide us with competitive advantages to continue expanding our cloud computing services in the future.

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As an integrated telecom service provider, we are providing and continuing to develop integrated services. For example, we have integrated our internal resources to offer cross-platform services over our broadband, mobile and internet platforms. These integrated services allow our customers to access our services, such as our multimedia programs, through a variety of terminals and devices.

Marketing, Sales and Distribution

Marketing Strategy

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

Services, Products and Bundled Offerings. We continually develop new value-added services and products, and bundle our services and products based on different market segments, with the aim of increasing our high-usage customers and enhancing customer loyalty. For example, we entered into an agreement with Apple Inc. and are currently a reseller of the iPhone in Taiwan. The iPhone combined with our mPro service helps retain existing customers and generate revenues through the increased use of our value-added services. In addition, we exempt deposits that we collect from specific mobile subscribers in advance for bundling subsidized mobile handsets with service plans.

Pricing and Promotions. We design flexible pricing packages that allow customers to select structures best tailored to their usage patterns, and design special promotional packages to encourage usage. For example, we have provided Let s Talk , My Hotline and Triple Save promotion packages to attract mobile customers.

Distribution Channels. We seek to facilitate customer subscription by adding more service points. In addition, we seek to broaden our distribution reach by strengthening our cross-industry alliances and marketing relationships. Furthermore, we seek to expand our sales channels by implementation of a sales agent system. In 2009, we began a collaboration with Tsann Kuen Trans-Nation Group, allowing the registration of mobile numbers at electronics stores for the first time, effectively increasing our points of sale. We also developed staff incentive programs to better motivate our sales staff.

Business Customers. We expanded our customer focus to include small and medium-sized enterprises in addition to large corporations. We seek to serve the needs of large corporate customers by devoting a project manager or project engineer to service these customers. These account managers are responsible for developing customized solutions and tariff packages to meet the specific needs of our customers. We continually update and expand our service offerings so that we can remain a one-stop telecommunications services provider to our corporate customers and provide for all of their telecommunications needs. Our dedicated local teams serve the needs of small and medium-sized enterprises. These teams also use our data bank to identify and target potential clients for promoting our e-commerce and mobile services. In addition, we help our corporate customers improve their efficiency and competitiveness by creating information systems for them.

Advertising. We are committed to further strengthening the Chunghwa Telecom brand and image as well as strengthening and expanding market recognition of our specialized product brands, such as HiNet and emome. We plan to leverage our leading market position and status to strengthen the overall advantage of our product brands.

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Sales and Distribution

Our marketing department at our corporate headquarters in Taipei is responsible for central business planning and formulating our marketing strategies and objectives. We have multiple marketing departments for our various businesses which are responsible for business and marketing planning.

As of December 31, 2012, we also had 17 operations offices, 392 service centers, 238 exclusive service stores and 6 customer service call centers located throughout Taiwan that are responsible for operations, sales and customer service in their respective local areas.

Customer Service and Billing

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

We provide the following services to our customers:

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

Network Infrastructure

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

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

Approximately 13,840 of our employees were engaged in network infrastructure development, maintenance, operation and planning as of December 31, 2012.

Transmission Networks

As of December 31, 2012, our transmission networks consisted of approximately 1.4 million fiber kilometers of fiber optic cable for trunking and approximately 5.84 million fiber kilometers of fiber optic cable for local loop.

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Synchronous digital hierarchy, or SDH, architecture is an advanced technology that allows for instantaneous rerouting and eliminates downtime in the event of a fiber cut. In addition, SDH offers better reliability and performance for optical fiber transmissions at a lower operating cost. In December 2002, we installed synchronous transport module 64 or STM 64, multiplexer and 32-wavelength dense wavelength division multiplexing, or DWDM, equipment on our long-haul backbone network. Our STM 64 multiplexer can multiplex several low speed signals into a 10 gigabits per second, or Gbps, high-speed signal. DWDM equipment uses a technology that puts data from different sources together on an optical fiber with each signal carried on its own separate wavelength. Both STM 64 multiplexer and DWDM equipment can increase our network capacity. Between 2007 and 2012, we deployed 40/80-wavelength Re-configurable Optical Add-Drop Multiplexer, or ROADM, for backbone transmission network in order to provide new data services such as gigabit Ethernet, fiber channel, 2.5 gigabit and 10 gigabit packet over SDH and 10 gigabit Ethernet. We have already completed the deployment of 892 wavelength ROADM by the end of 2012. To meet the demand for broadband services, we will install an optical cross-connect, or OXC, network and a next generation synchronous digital hierarchy, or NG SDH, network, which provides gigabit Ethernet over SDH service, between 2009 and 2013. We have already completed the deployment of 4,385 GbE OXC/NG SDH by the end of 2012.

Based on the transmission network described above, we have been providing connection circuit service of 10 gigabit packet over SDH and 10 gigabit Ethernet to the government s Taiwan Advanced Research and Education Network since November 2006 and will continue the service until November 2013.

As part of our strategic focus on the internet and data markets, our local loop connections use ADSL technology. This enables us to deliver high-speed internet, multimedia and other data services to our customers. Substantially all of our installed telephone lines are capable of delivering ADSL services. As of December 31, 2012, we had approximately 3.87 million lines of ADSL and had 1.8 million ADSL customers. In addition, the Ethernet-based FTTx system is also introduced into our access network to provide broadband services, such as MOD, high speed internet access and VPN. As of December 31, 2012, we have constructed approximately 4.75 million FTTx ports and had 2.7 million FTTx customers. Our FTTx service can offer high-speed broadband internet access rates up to 1Gbps.

Switching Networks

Domestic telecommunications network. Our domestic public switched telephone network currently consists of 19 message areas connected by a long distance network. As of December 31, 2012, we had 38 long distance exchanges, which are interconnection points between our telecommunications network and approximately 17.5 million telephone lines, which reached virtually all homes and businesses in Taiwan.

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

As of December 31, 2012, our NGN core network consisted of 985,500 local telephone subscribers, comprising 448,000 Session Initiation Protocol-based, or SIP-based, and 537,500 Access Gateway-based, or AG-based, subscribers.

Our NGN Managed IP backbone network consists of an inner core network and an outer core network. We completed the construction of our high-speed NGN Managed IP backbone network at the end of 2012 with 12 sets of 1.6 Tbps/640 Gbps switch routers for the inner core network and more than 26 sets of 1.6 Tbps/640 Gbps switch routers for the outer core network. The bandwidth of the network is approximately 755 Gbps as of the end of 2012. We believe this network will enable us to meet the increasing demand for NGN services, such as VoIP, and all managed services, including MOD and VPN.

International network. Our international transmission infrastructure consists of both submarine cable and satellite transmission systems, which link our national network directly to 100 telecommunications service providers in 43 international destinations.

International calls are routed between Taiwan and international destinations through one of our two international switching centers, one located in Taipei and the other in Kaohsiung. Each center had two time-division multiplexing, or TDM, international gateway switches and two NGN international gateway switch. We had a trunk capacity of 133,040 channels in total as of December 31, 2012.

As of December 31, 2012, we had invested in 16 submarine cables, seven of which land in Taiwan. We had increased the capacity of each of our current submarine cables, increasing our aggregate total capacity from 1,058 Gbps in 2011 to 1,208 Gbps in 2012.

Mobile Services Network

Our mobile services network consists of:

- cell sites, which are physical locations equipped with a base station consisting of transmitters, receivers and other equipment used to communicate through radio channels with customers mobile handsets within the range of a cell;
- BSC (base station controllers) for GSM or RNC (radio network controller) for 3G, which connect to, and control , the base station within each cell site;
- cellular switching service centers, which control the base station controllers and the processing and routing of telephone calls;
- GGSN (gateway GPRS support nodes), which connect our GPRS network to the internet;
- SGSN (serving GPRS support nodes), which connect the GPRS network to the base station controllers; and
- transmission lines, which link (i) with respect to the GSM or 3G network, the mobile switching service centers, base station controllers, base stations and the public switched telephone network, and (ii) with respect to the GPRS network, the base station controllers, the support nodes and the internet.

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

	As of December 31,		
	2010	**2011**	**2012**
GSM system			
GSM base stations	9,336	9,531	9,557
Switches	44	44	44
Lines of capacity (in thousands)	6,500	6,500	5,800
Taiwan population coverage	99.9%	99.9%	99.9%
3G system			
3G base stations	6,879	8,442	10,384
Servers / gateways	8/16	8/16	8/16
Lines of capacity (in thousands)	3,450	4,400	4,400
Taiwan population coverage	94.5%	95.8%	98%
System (Home Location Register) capacity (in thousands)	7,200	7,200	7,600

As of December 31,

	2012
Packet-switched system after consolidation of GSM and 3G	
GPRS gateway support nodes	14
Direct IP access locations / capacity (in Gbps)	8/46.6
Serving support nodes	12

We provide mobile services based on the GSM network standards. We have the 900 MHz and 1800 MHz frequency bands paired with spectrums of 15 MHz and 11.25 MHz, respectively, for our GSM services. As of December 31, 2012, we had constructed 9,557 base stations, providing up to 99.9% population coverage. Since the launch of our 3G mobile services, we have gradually transitioned GSM subscribers to 3G and have started to consolidate our GSM network.

We have installed an intelligent network on our mobile services network infrastructure to enable us to provide prepaid services as well as a wide range of advanced call features and value-added services. As of the end of 2012, our intelligent network capacity reached 1.12 million prepaid customers and 1.01 million mobile virtual private network customers.

We have 15 MHz paired spectrum plus 5 MHz unpaired spectrum in the 2 GHz frequency band for our 3G mobile services, which was launched in July 2005. We contracted with Nokia Siemens Networks to provide the core network, radio access network, service network, transmission network and maintenance network for our 3G network. To promote mobile internet use, we upgraded our network to 3.5G in September 2006, with downlink and uplink speeds of 7.2 Mbps and 2.0 Mbps, respectively. To meet the high growth in mobile data traffic, we have upgraded our existing High-Speed Packet Access (HSPA with capability of 14.4 Mbps and 5.76 Mbps each for Down-link and Up-link) Network to HSPA+ (with capability of 21.6 Mbps and 11.5 Mbps each for Down-link and Up-link). As of December 31, 2012, we had completed the construction of about 10,384 3G base stations with 6.7 million subscribers.

In order to operate our packet-switched network more efficiently, we have consolidated GSM and 3G serving GPRS support nodes (SGSN) into a single core network. We have also introduced the Direct Tunnel technology to flatten the packet-switched network to enhance the user s experience.

Internet Network

HiNet, our internet service provider, has the largest internet access network in Taiwan, with 33 points of presence approximately 5,572,000 broadband remote access server ports and a backbone bandwidth of approximately 2,310 Gbps as of December 31, 2012. We plan to increase HiNet s points of presence and backbone bandwidth to approximately 3,100 Gbps by the end of 2013.

HiNet s broadband backbone network consists of an inner core network and an outer core network. We completed the construction of our high-speed internet protocol backbone network at the end of 2012 with 16 sets of 7.04Tbps/4.48Tbps/1.6Tbps/1.28Tbps switch routers for the inner core network and more than 50 sets of 2.64Tbps/1.6Tbps/1.28Tbps/880Gbps/640Gbps/320Gbps switch routers for the outer core network. We believe this network will enable us to meet the increasing demand for our internet services.

HiNet s total international connection bandwidth is 423 Gbps as of December 31, 2012. As we expect that internet traffic flows to and from the United States will continue to increase, we plan to expand our bandwidth to the United States. We also plan to increase our links to other countries, including Japan, Korea, Hong Kong, Singapore, Mainland China, Malaysia and Thailand.

Leased Line and Data Switching Networks

We operate leased line networks on both a managed and unmanaged basis. In addition, we operate a number of switched digital networks used principally for the provision of packet-switched, frame relay, asynchronous transfer mode technology and a multi-protocol label switching internet protocol VPN. We have completed the construction of a digital cross connect system for provisioning and managing voice-grade data services throughout Taiwan with a total of 50 nodes. As of December 31, 2012, we had 1,088 frame relay ports, 1,819 asynchronous transfer mode ports and approximately 72,334 multi-protocol label switching internet protocol VPN virtual ports.

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

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Competition

We face competition in virtually all aspects of our business.

Domestic Fixed Communications

We were the largest domestic fixed communications service provider in Taiwan, with a market share of approximately 95.0% in terms of customers for local telephone services, approximately 75.4% in terms of traffic for domestic long distance telephone services, and approximately 79.2% share of the broadband internet access market in terms of customers in 2012, respectively. Three providers, namely, Taiwan Fixed Network, New Century Infocomm Tech. Co., Ltd. and Asia Pacific Telecom Co. Ltd., have provided fixed communication services since June 2001. Our domestic long distance services compete with mobile services as people increasingly use mobile handsets. We believe that the fixed-line competition in Taiwan will be primarily based on price, quality of service, network coverage and customer services, such as call centers and unified billing.

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

Our primary competitors in leased line services and broadband services include:

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

- Broadband internet access providers: kbro Co., Ltd., Taiwan Fixed Network and New Century Infocomm Tech. Co., Ltd., China Network System Co., Ltd.; and

- Cable operators: kbro Co., Ltd., China Network Systems Co., Ltd., Taiwan Broadband Communications Co., Ltd., Pacific Broadband Co., Ltd., and Taiwan Infrastructure Technology Co., Ltd.

Mobile Communications

There are currently three major GSM mobile operators in Taiwan, namely, Taiwan Mobile Co., Ltd., FarEasTone Telecommunications Co., Ltd. and us. Based on data provided by the NCC, as of December 31, 2012, we were the largest mobile operator in Taiwan, with a 59.5% market share in terms of 2G customers. Smart phones with 3G mobile data packages are becoming popular in recent years. To attract more high-end data users, all three major operators offer free intra-network calling packages bundled with mobile data service. Also, there are two 3G mobile operators in Taiwan in addition to us, namely Asia Pacific Telecom Co., Ltd. and Vibo Telecom Inc., as well as one personal handyphone system operator, First International Telecom. Furthermore, the government issued a total of 16 mobile virtual network operator, or MVNO, licenses, which allow operators without a spectrum allocation to provide mobile services by leasing the capacity and facilities of a mobile service network from a licensed mobile service provider. We are currently cooperating with Carrefour Telecom Co., Ltd. We may cooperate with other mobile virtual network operators in the future. As of the end of 2012, there were also six WiMAX service providers in Taiwan, providing services to approximately 137,009 customers in total according to the data provided by the NCC. We compete in the wireless services market primarily on the basis of price, quality of service, network reliability and attractiveness of service packages.

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Internet

Our primary competitors in internet services are other internet services providers, including SeedNet, TWM Broadband.

We are the largest provider of internet services in Taiwan. As of December 31, 2012, we had a 69.6% share of the Taiwanese internet service market in terms of customers. We compete in the internet services market primarily on the basis of price, technology, speed of transmission, amount of bandwidth available for use, network coverage and value-added services.

International Fixed Communications

We are the largest international fixed communications service provider in Taiwan, with a market share of approximately 51.0% in terms of traffic for international long distance telephone services in 2012. Three new providers, namely, Taiwan Fixed Network, New Century Infocomm Tech. Co., Ltd. and Asia Pacific Telecom Co. Ltd., have provided fixed-line services since June 2001. We believe these operators are primarily focused on international long distance services. In addition, we anticipate that these operators will focus on corporate customers, which typically generate higher profit margins than residential customers. Since August 2001, four undersea cable services licenses have been granted. These undersea cable operators, as well as internet service providers and international simple resale operators, have begun offering international leased line services to other fixed-line operators, internet service providers and international simple resale operators.

Our international long distance services compete with international long distance resale services and alternative mediums for making international calls, including VoIP technologies, such as those provided by Skype.

Cyber Security and Personal Information Protection

To prevent increasing cyber risks and threats, recently we have implemented the following mechanisms:

- We have built an online service system which enables Certificate Authority s Secure Socket Layer functions that performs as a secure tunnel to transmit encrypted customer s information. In addition, we offered the Global Trust Secure Site Seal to protect from phishing attacks on payment web sites.

- The High-Availability systems in our data centers deploy firewall and Intrusion Prevention System, or IPS, to defend against hackers attacks, and the web application programs enforce penetration test to ensure the security of our customers information.

- The network equipment in our data centers could distinguish DDoS threats and reject or block the attacks. In the future, we could even block the DDoS traffic over the backbone network.

On May 26, 2010, the President of the Republic of China announced the amendment of the Personal Information Protection Act, or PIPA, which became fully effective on October 1, 2012, except for its Articles 6 and 54 that await further determination by the Executive Yuan. PIPA applies to all individuals, legal entities and enterprises that collect, process and use personal information, and has a significant impact on the banking and service industries in Taiwan. Due to the adoption of PIPA, the level of responsibility and liability on personal information protection of a company was raised. We have conducted inventory checks of personal information that we currently hold, established standard operating procedures, or SOP, to comply with the requirements under PIPA, and have taken information security measures to protect the data.

To comply with the PIPA, we implemented a series of measures to avoid customer information leakage:

- The customer information systems have been enforced on firewall and IPS to avoid hacker s attacks.

- Regular internal audit: Our auditing department completes an annual audit plan and regularly audits information circulation in each department on customer information management and protection.

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External consulting: We, in accordance with the PIPA, request accounting firms not performing audit service for us to conduct external consulting every year on customer information management and protection.

Documents containing customer s personal information are labeled highly confidential. All levels of managers shall monitor the usage of customers personal information by employees.

Properties

Our properties consist mainly of land, land improvements and buildings located throughout Taiwan. We own approximately 411 hectares of land and 3.5 million square meters of building floor space. In January 2008, we established Light Era Development Co., Ltd. for the purpose of developing our real estate properties. As of December 31, 2012, we have transferred six properties to Light Era Development Co., Ltd. The development work on five of these properties is completed. Light Era Development Co., Ltd. further acquired land located near the high speed rail station in Taoyuan, from a private party in October 2012. This property will be used to develop smart residential buildings. We plan to deploy state-of-the-art technologies including fiber broadband, ICT services, energy saving technologies and remote surveillance service technologies in these intelligent residential buildings. Following the gradual completion of land rezoning, we have focused our real estate development more towards multiuse and diverse projects. Hence, we have developed more properties for commercial use and participated in government urban redevelopment plans. We have received approximately NT$608 million (US$20.9 million) in rental income in 2012 from such properties.

Insurance

We do not carry comprehensive insurance for our properties or any insurance for business disruptions. We do, however, maintain in-transit insurance for key materials, such as cables, equipment and equipment components. We do not carry insurance for the ST-2 satellite since we only lease capacity for our operations instead of owning the satellite.

Employees

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

Our Pension Plans

Currently, we offer two types of employee retirement plans our defined contributions plan and defined benefits plan which are administered in accordance with the Republic of China Labor Standards Act and the Republic of China Labor Pension Act.

Legal Proceedings

A portion of the land used by us during the period between July 1, 1996 and December 31, 2004 was jointly owned by us and Chunghwa Post Co., Ltd., Directorate General of Postal Service. In accordance with the claims process in Taiwan, on July 12, 2005, the Taiwan Taipei District Court sent a claim notice to us requiring us to reimburse Chunghwa Post Co., Ltd. in the amount of NT$768.0 million for land usage compensation due to the portion of land usage area in excess of our ownership, along with interest calculated at 5% interest rate from June 30, 2005 to the payment date. However, we believe that both parties have the right to use co-managed land without consideration and thus Chunghwa Post Co., Ltd. does not have the right to request land compensation payments. Furthermore, we also believe that the computation used to derive the land usage compensation amount is inaccurate because most of the compensation amount has expired as a result of the expiration clause. On March 30, 2009, the Taiwan Taipei District Court rendered its judgment that we only need to pay approximately NT$17 million, along with interest calculated at 5% per annum from July 23, 2005, and 4% of Chunghwa Post Co., Ltd. s court fees as compensation. Chunghwa Post Co., Ltd. appealed to the Taiwan High Court on April 22, 2009. We also filed an appeal to the Taiwan High Court within the statutory period. On April 7, 2010, the Taiwan High Court rendered its judgment, ruling that we need to pay approximately NT$23 million, in addition to the approximately NT$17 million from the Taiwan Taipei District Court judgment, along with interest calculated at 5% per annum from July 23, 2005, and 12.5% of Chunghwa Post Co., Ltd. s court fees from its original suit and subsequent appeal as compensation. We filed an appeal with the Supreme Court on April 22, 2010 and the Supreme Court reversed and remanded the judgment for a new trial at Taiwan High Court in June 2011. On January 6, 2012, the Taiwan High Court ruled that we need to pay NT$4 million (US$0.1 million) to Chunghwa Post Co., Ltd., in addition to the amount as demanded by court in the Taipei District Court judgment, along with interest calculated at 5% per annum from July 23, 2005. The decision of the court is final, and we made the payment in full accordingly by the end of 2012.

We are involved in various legal proceedings of a nature considered in the ordinary course of our business. It is our policy to provide for reserves related to these legal matters when it is probable that a liability has been incurred and the amount is reasonably estimable.

We believe that the various asserted claims and litigation in which we are involved will not materially affect our financial condition or results of operations although no assurance can be given with respect to the ultimate outcome of any such claim or litigation.

Capital Expenditures

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

Enforceability of Judgments in Taiwan

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

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

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

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Regulation

Overview

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

Regulatory Authorities

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

On January 9, 2008, an announcement issued by the President amended the Organization Law, or New Amendment, amending the unconstitutional formation articles and reducing the total number of commissioners to seven with a term of four years, but three of the commissioners appointed after the New Amendment serve a term of two years. The commissioners will be nominated by the premier of the Executive Yuan and approved and appointed by the Legislative Yuan.

The new nomination method under the New Amendment became effective on February 1, 2008 when the Legislative Yuan started its new term. The nine incumbent commissioners continued to serve until July 31, 2008, when their terms ended. The premier of the Executive Yuan nominated seven commissioners on July 1, 2008, and they were approved and appointed by the Legislative Yuan on July 18, 2008. The new commissioners took office on August 1, 2008. Thereafter, upon the resignation of one commissioner and the expiry of the term for the three commissioners, four new commissioners were nominated by the premier of the Executive Yuan, approved and appointed by the Legislative Yuan and began serving as commissioners on August 1, 2010. The Organization Law was further amended on December 28, 2011. The amendment stipulates that the premier of the Executive Yuan shall appoint one Commissioner to serve as Chairperson, and one as Vice Chairperson upon nomination of the commissioners. Accordingly, the Chairperson, the Vice Chairperson and two new Commissioners were nominated by the premier on April 30, 2012, approved and appointed by the Legislative Yuan and began tenure as commissioners on August 1, 2012.

In accordance with the Organization Law, the NCC is responsible for:

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

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

Telecommunications Act

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

- licensing of telecommunications services;
- telecommunication numbers;
- restrictions on dominant telecommunications service providers;
- tariff control and price cap regulation;
- accounting separation system;
- interconnection arrangements;

bottleneck facilities;

spectrum allocation;

provision of universal services;

equal access;

number portability;

local loop unbundling;

co-location; and

ownership limitations.

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

Licensing of Telecommunications Services

Type I and Type II Service Providers

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

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

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

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

Commencing in 2007, the NCC began accepting applications for licenses to provide fixed-line services in March, June, September and December of each year. The NCC started to accept applications for fixed-line services on a daily basis beginning in 2008. There is no limit on the number of fixed-line licenses that they may decide to issue.

Granting of Licenses

Type I

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

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

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

The Telecommunications Act further authorizes the competent authority, now the NCC, to promulgate separate regulations governing each Type I service, including the business scope of the Type I service provider, as well as the procedures and conditions for granting special permits and the length of the period of the special permits of each Type I service. Each holder of a Type I license will pay a fee ranging from 0.5% to 2% of or their bid price ratio (Article 2 of the Type I Service Provider Special Tariff Standards) multiplied by their annual revenues generated from the particular Type I service for which a license has been granted.

Fixed-line Services. Under the Telecommunications Act, the Fixed Network Regulations govern the issuance of fixed-line service licenses and the business scope of fixed-line providers. Fixed-line service licenses are subdivided into the following categories:

- integrated services, including local, domestic long distance, international long distance telephone services;
- local telephone services;
- domestic long distance telephone services;
- international long distance telephone services; and
- local, domestic long distance and international long distance leased line services. We conduct our fixed-line services through a license for integrated services.

Licenses for local telephone and integrated services are valid for 25 years. Licenses for domestic long distance and international long distance telephone services are valid for 20 years. Licenses for leased line services are valid for 15 years. If the service provider wishes to continue operating, the service provider needs to apply for a license renewal to the NCC between nine months and six months before the expiration of their license. The minimum paid-in capital requirements for integrated services providers that applied for a license before June 30, 2004, between July 1, 2004 and January 31, 2008 and on or after February 1, 2008 are NT$21 billion, NT$8.4 billion and NT$6.4 billion, respectively. The minimum paid-in capital requirements for both domestic and international long distance telephone service providers that applied for a license between July 1, 2004 and January 31, 2008 and on or after February 1, 2008 are NT$1.05 billion and NT$800 million, respectively. The minimum paid-in capital requirements for international undersea leased cable service providers that applied for a license before June 30, 2004, between July 1, 2004 and January 31, 2008 and on or after February 1, 2008 are NT$420 million, NT$420 million and NT$320 million, respectively. The minimum paid-in capital requirement for local telephone service providers that applied for a license between July 1, 2004 and January 31, 2008 and on or after February 1, 2008 are NT$6.3 billion and NT$4.8 billion, respectively, multiplied by the Local Network Operation Weights for the regions in which local network managerial rights have been granted to the service provider. The Local Network Operation Weights are calculated as the population of the region as a proportion of the entire population of Taiwan and are announced by the competent authority every three years. If an applicant for a license is also a Type I service provider, it will need to combine the minimum paid-in-capital requirements for all relevant services.

In March 2000, the government granted three new concessions to fixed-line services providers for integrated services. Recipients of these concessions are required to apply for a network construction permit to deploy broadband local access networks. Each recipient of these concessions is required to have capacity for 150,000 customers before it is able to apply for a fixed-line license to launch its proposed services. The three fixed-line service providers have since obtained fixed-line licenses and are required to achieve capacity for one million customers by the sixth year following the date of the grant of the network construction permit awarded. Operators that applied for integrated service provider licenses before June 30, 2004, between July 1, 2004 and January 31, 2008 and on or after February 1, 2008 must achieve a capacity for 1.0 million, 0.4 million and 0.3 million customers, ports or a combination of both, respectively, by the fourth year following the date of the grant of the network construction permit.

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

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

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

The wireless service license for mobile or paging service, once granted, should be valid for a term of 15 years starting from the date when such license is granted, and licenses for mobile data, digital low-power cordless telephone and trunked radio are valid for 10 years starting from the date when such license is granted. According to the Regulations for Administration of Mobile Communications Businesses amended by the NCC on September 19, 2011, the wireless service provider may file an application with the NCC for extension of the valid term of its license for providing mobile or paging service one year prior to the expiry of the 15-year valid term. Once the NCC approves the application, the valid term of the wireless service license for mobile or paging service will be extended to June 30, 2017. The valid terms of our licenses granted by the ROC government authorities for providing 2G mobile services on the 900MHz and 1800MHz spectrum will expire in 2012 and 2013 respectively. We filed the application with the NCC for extending the valid terms of our 2G licenses on November 29, 2011. Our application was approved by the NCC in November 2012 and the terms of our licenses for providing 2G mobile services on the 900MHz and 1800MHz spectrum should be valid until June 2017.

The minimum paid-in capital requirements for different mobile communication businesses are as follows: Digital Low-Power Wireless Telephone Business, NT$200 million; Trunking Wireless Telephone Business, NT$20 million for regional operation and NT$60 million for island-wide operation; Mobile Data Communication Business, NT$50 million for regional operation and NT$150 million for island-wide operation; Radio Paging Business, NT$200 million for regional operation and NT$400 million for island-wide operation; Mobile Telephone Business, NT$2 billion for regional operation and NT$6 billion for island-wide operation. If one single applicant acquires operational licenses of two or more businesses with minimum paid-in capital requirements, the paid-in capital for the businesses should be calculated and collected by the applicant separately.

For an operator who obtains the permission of operation over two businesses through the legal procedure, its minimum paid-in capital shall be separately calculated upon approval for establishment, if such other businesses are subject to the minimum paid-in capital restriction.

Third Generation Mobile Services. The Ministry of Transportation and Communications promulgated the Third Generation Mobile Telecommunications Services Regulations on October 15, 2001. The NCC amended the above regulations on July 5, 2007, designating itself as the authority in charge of the third generation, or 3G, mobile services regulations and further amended such regulations on December 30, 2008 for the establishment of base stations. The regulations govern voice and non-voice telecommunications services provided using the spectrum assigned by the Ministry of Transportation and Communications, and now governed by the NCC, that utilizes the IMT-2000 technical standards as announced by the International Telecommunications Union. Licenses for 3G mobile services were granted by the Ministry of Transportation and Communications and are now granted by the NCC. We have received our 3G mobile services license, which is valid from May 26, 2005 to December 31, 2018.

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Under the Third Generation Mobile Telecommunications Services Regulations, the operation area of this business is the whole nation; the minimal paid-in capital for operating this business shall be NT$6 billion. If the applicant operates another business of a Type I telecommunications enterprise at the same time and there is a restriction on the paid-in capital to the other business, after acquiring the establishment approval, the required minimal paid-in capital shall be calculated by aggregating the minimal requirement of each service. A company holding a 3G mobile license and having 200 or more shareholders is required to become a public company, which is subject to the stringent disclosure requirements under the securities regulations of the ROC A company holding a 3G mobile license is also required to submit a report to the NCC within 20 days after its shareholders approve the capital reduction of such company, the entering into, modification or termination of any contracts regarding leasing of all business, outsourcing of operations or joint operations, the transfer of the whole or substantial part of the business or assets of such company, and taking over of the whole of the business or assets of any other company which would have a significant impact on such company s operations.

Satellite Services. Under the Telecommunications Act, the Satellite Regulations promulgated by the Ministry of Transportation and Communications govern the issuance of satellite services licenses and the business scope of satellite service providers. The NCC amended the above regulations on July 20, 2007, designating itself as the authority in charge of the Satellite Regulations. Satellite services licenses are subdivided into fixed satellite services licenses and mobile satellite services licenses.

The satellite services license should be valid for a term of 10 years starting from the date when such license is granted. If the service provider wants to re-new its satellite services license before the expiry of the 10-year term, such service provider needs to file a renew application with the NCC within the period from 9 months to 6 months before the expiry date of the original satellite license. The valid term of the renewed satellite license will be 10 years. Minimum paid-in capital requirements for fixed satellite services providers and mobile satellite services providers are NT$100 million and NT$500 million, respectively.

We currently hold a fixed satellite services license, valid from December 10, 2008 to December 9, 2018.

Type II

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

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

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

Under regulations governing the fees payable for Type II licenses, operators of simple resale or network telephone services of E.164 or non-E.164 user numbers must pay an annual license fee equal to 1% of annual revenues generated from these services during the previous year. Type II service operators providing services other than simple resale or network telephone services of E.164 or non-E.164 user numbers must pay license fees ranging from NT$6,000 to NT$150,000 depending on their respective paid-in capital. For operators who operate over two or more businesses, their license fee shall be separately calculated but jointly collected. The regulations do not apply to integrated services providers who are permitted to provide Type II services without additional Type II Licenses.

The Directorate General of Telecommunications started to process the applications for allocating E.164 and non-E.164 user numbers (IP phone numbers) on November 15, 2005. A few operators, including our company, have applied for IP phone numbers. We applied to the NCC for E.164 user numbers and as of January 30, 2008, we have received approval to build a network with a capacity of 30,000 numbers. As we are governed by fixed-line regulations, we need to receive approval from the NCC for our operation rules, tariff and service agreement for IP phone numbers before we can commence E.164 service. We filed with NCC to return 30,000 E.164 numbers, and the application was approved by the NCC on July 1, 2011. Please refer to B. Business Overview for further discussion.

Telecommunications Numbers

According to the Telecommunications Act, numbering codes, subscriber numbers, identification numbers and other telecommunication numbers will be distributed and managed by the NCC. These telecommunication numbers may not be used or changed without approval by the NCC. In order to maintain effective use of available telecommunication numbers, the Telecommunications Act empowers the NCC to reallocate and retrieve and to collect a usage fee for distributed telecommunication numbers. The NCC promulgated the Fee Standards for Special Telecommunication Numbers on March 18, 2010, effective immediately, requiring telecommunications service providers to pay 70% of revenues collected from the auctioning off and selection of golden numbers and the standard usage rates for special identification numbers in use.

Restrictions on Dominant Telecommunications Services Providers

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

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

We have been declared by the former competent authority Ministry of Transportation and Communications as a dominant Type I service provider for fixed-line and GSM mobile services. On July 7, 2012, we have been classified as a dominant Type I service provider for 3G mobile services by the NCC. Under the Telecommunications Act, a dominant Type I service provider must not engage in the following activities:

- directly or indirectly hinder a request for interconnection with its proprietary technology by other Type I service providers;
- refuse to release to other Type I service providers the calculation methods of its interconnection fees and other relevant materials;

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- improperly determine, maintain or change its tariffs or means of services;
- reject, without due cause, a request for leasing network components by other Type I service providers;
- reject, without due cause, a request for leasing lines by other service providers or customers;
- reject, without due cause, a request for negotiation or testing by other service providers or customers;
- reject, without due cause, a request for negotiation for co-location by other service providers;
- discriminate, without due cause, against other service providers or customers; or
- abuse its position as a dominant provider, or engage in other unfair competition activities as determined by the regulatory authorities.

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

Tariff Control and Price Cap Regulation

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

Under the Administrative Regulations Governing Tariffs of Type I Telecommunications Enterprises, a dominant Type I service provider must submit its proposed adjustment in primary tariffs and promotional packages to the NCC for approval at least 14 days prior to the date of the proposed tariff changes and announce such change on media, website and business locations on the day after the NCC grants the approval. The tariff change will come into effect seven days after the announcement.

Primary tariffs include:

- for fixed-line local telephone services: monthly fees, usage fees, monthly rental fees of leased lines and pay telephone usage fees;
- for fixed-line domestic long distance telephone services: usage fees and monthly rental fees of leased lines;
- for fixed-line international long distance telephone services: usage fees and leased line monthly rental fees;
- for wireless services, including 3G mobile services: monthly rental fees and usage fees;
- for internet services provided by dominant Type I service providers: connection and usage fees; and

other fees or tariffs announced by the Directorate General of Telecommunications before March 1, 2006 or by the NCC from March 1, 2006.

In addition, a dominant Type I service provider is required to set wholesale prices for the provision of its telecommunication services to other telecommunication enterprises. These telecommunication services and their suitable targets, all of which are subject to annual reviews by the NCC, include:

interface circuits (local and long distance) between internet access service providers and customers for Type I and Type II service providers

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- interface circuits (local and long distance) between internet access service providers for Type I and Type II service providers that are internet access service providers

- interconnection circuits between Type I service providers and between Type I and Type II service providers of international simple resale, or ISR, and E.164 VoIP services

- DSL-family (xDSL) circuits for fixed-line service providers and internet service providers

- other local and long distance data circuits for Type I and Type II service providers

- broadband internet interconnection for Type I and Type II service providers that are internet access service providers.

The initial wholesale prices set by a dominant Type I service provider may be the retail price less fees and expenses which need not be incurred, but shall not be higher than its promotional pricing. Changes in the wholesale price charged by a dominant Type I service provider may not be greater than (i) the retail price less fees and expenses which need not to be incurred but not greater than the promotional pricing; or (ii) the annual growth rate of the consumer price index in Taiwan minus the constant set by the NCC, whichever is the lower. The Administrative Regulations Governing Tariffs of Type I Telecommunications Enterprises further prohibits a dominant Type I service provider from practicing unfair competition against other telecommunication enterprises.

In comparison, all non-dominant Type I service providers are required to notify the NCC and the public of their proposed tariff adjustments seven days prior to the date of the proposed tariff change with respect to all tariffs. In addition, changes in tariffs charged by Type I service providers (notwithstanding the type of their respective services) may not, in any event, be greater than the annual growth rate of the consumer price index in Taiwan adjusted by an adjustment coefficient, which will be periodically determined and announced by the NCC. For example, if:

- the annual growth rate of the consumer price index in Taiwan minus the adjustment coefficient is positive, the increased percentage of tariffs must not exceed such positive figure;

- the annual growth rate of the consumer price index in Taiwan minus the adjustment coefficient is negative, the decreased percentage of tariffs must be at least the absolute value of such negative figure, and the tariffs used in the given year must not be higher than the decreased tariff; and

- the annual growth rate of the consumer price index in Taiwan minus the adjustment coefficient equals to zero, no increase in tariffs is allowed to be made by any Type I service providers.

On January 29, 2010, the NCC announced that effective April 1, 2010 to March 31, 2013:

- the adjustment coefficient to be applied to the tariff adjustment for the fixed-line integrated services is 4.816% and covers the following:

  - dominant providers of fixed-line services

  - tariffs of the following:

the monthly fee for ADSL leased line and the usage fee for domestic long distance telephone services (excluding public pay phones)

wholesale prices of the following:

the monthly fee for leased lines services (including local and domestic long distance leased lines) between internet service providers and their customers

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the monthly fee for leased lines services (including local and domestic long distance leased lines) between an internet service provider and another internet service provider

the monthly fee for the interconnection (including local and domestic long distance lines) between a Type 1 telecommunication service provider and another Type 1 telecommunication service provider; the monthly fee for the interconnection (including local and domestic long distance lines) between a Type 1 telecommunication service provider and a Type 2 telecommunication service provider who provides simple resale and network telephone service of E.164 user numbers.

the monthly fee for other local and domestic long distance leased lines

the interconnection fee for internet bandwidth interconnection

no adjustment coefficient will be applied to the call charges for the domestic fixed communication services during the following periods:

the integrated services operators and the domestic telephone services operators can determine the tariff adjustment for the domestic telephone services during the specific period and seek NCC s approval or recognition

the specific periods include 11.00pm to 8.00am from Monday to Friday, 12.00am Saturday to 8.00am Monday, and the whole day of a national holidays

the adjustment coefficient to be applied to the tariff adjustment for the mobile services and the 3G mobile services is 5% and covers the following:

2G mobile service and 3G mobile service operators

tariffs of the following:

domestic short messaging services

calls made from a 2G mobile services customer or from a 3G service network to a domestic fixed communication network

calls made from a 2G mobile services customer or from a 3G service network to a 2G mobile service network, a 3G mobile service network, a 1900MHz Digital Low-Tier Cordless Telephone Services, or PHS, or WiMAX services the adjustment coefficient to be applied to the cellular voice access charge will be announced separately after the amendment to the relevant regulations.

the adjustment coefficient to be applied to the tariff adjustment for other Type 1 telecommunication services is the annual growth rate of the consumer price index in Taiwan

The NCC required the service operators which are subject to the above tariff restrictions shall submit their tariff adjustment plans by March 12, 2010 to the NCC for approval. The NCC approved our tariff adjustment plan on March 24, 2010.

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Type II service providers are free to establish their own tariff schemes, but are required to notify the NCC and the public upon adoption and upon any subsequent adjustments. The NCC approved our tariff adjustment plan on March 24, 2010.

The NCC announced an amendment of Administrative Regulation Governing Tariffs of Type I Telecommunications Enterprises, other applicable regulations and the adjustment coefficient on February 7, 2013. The material amendments are set forth below:

- Only the dominate service provider will be subject to the restrictions on adjustment of the tariffs charged;
- The adjustment of retail tariff charged for communications of long distance networks, international networks, and mobile (except for mobile prepaid calling card) will no longer be subject to NCC s prior review and approval;
- The coefficient applied to calculate the amount of xDSL monthly rents for local and long distance network circuits and other five wholesale services provided by the dominant providers will be adjusted to 5.1749%, which means the amount of rents will decrease for the fourth straight year; and
- The amount of other primary tariffs charged by dominate service providers shall not be raised until March 31, 2017.

Accounting Separation System

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

Interconnection Arrangements

The Telecommunications Act requires all Type I service providers to allow other Type I service providers access to their networks. It further requires Type I service providers, within three months upon request by the other Type I service provider, to reach an agreement on the relevant terms for the interconnection. Prices charged for interconnection must be based on cost. If the parties fail to reach an agreement within three months, the NCC may, either at the request of the parties or on its own accord, arbitrate and determine the interconnection terms for the parties. The Telecommunications Act authorizes the Directorate General of Telecommunications or, from March 1, 2006, the NCC to issue rules and regulations pertaining to interconnection.

The Administrative Rules for Network Interconnection establishes the basis for determining the interconnection charge of a dominant Type I service provider, which shall be reviewed every four years. The interconnection charge of a dominant Type I service provider shall be reviewed by the NCC in advance, and the NCC has the right to modify the rate.

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A dominant Type I service provider shall unbundle its network elements. The unbundled network elements shall contain the following:

- local loops;
- local switch transmission equipment;
- local trunks;
- toll switch transmission equipment;
- long distance trunks;
- international switch transmission equipment;
- network interfaces;
- directory equipment and services; and
- signaling network equipment.

Unless otherwise provided by the laws, interconnection charge of the providers for mobile communications businesses and the 3G mobile communications business should be calculated based on the decrees issued by NCC. The foregoing shall apply, mutatis mutandis, to the calculation and reviewing method of the interconnection charge of the dominant providers for fixed communication services.

Unbundled network components of the providers for mobile communications businesses and the 3G mobile communications business include:

- mobile telecommunications trunks;
- mobile telecommunications base stations;
- controlling equipment of mobile telecommunications base stations;
- mobile telecommunications switch transmission equipment; and
- other items recognized by the NCC.

The Administrative Rules for Network Interconnection Between Telecommunication Service Providers was further amended by the NCC on November 2011 specifying the charges for network interconnection among Type I service providers as follow:

Before January 1, 2011, except for international communications, tariffs for communications between a mobile telecommunications network and a fixed-line network were collected from the call-originating subscribers by the call-originating service provider pursuant to the tariff schedules set by the mobile communication service provider, and revenues or any uncollectible accounts from such tariffs went to the mobile service provider. However, from January 1, 2011, although the tariffs shall still be paid by the call-originating subscribers, the tariff schedules are set by the call-originating network service provider, and revenues or any uncollectible accounts from such tariff shall go to the call-originating service provider. During the transition period from January 1, 2011 to December 31, 2016, we, as a dominant Type I fixed-line service provider, shall pay extra transition fee in addition to access charges to the mobile communications service providers.

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Tariffs for communications between mobile telecommunications networks shall be paid by the call-originating subscribers pursuant to the tariff schedules set by the call-originating service providers, and the revenues or any uncollectible accounts from such tariffs shall go to the call-originating service providers.

Tariffs for communications between fixed-line network will be determined by the following principles:

tariffs for communications between the local telephone networks shall be paid by the call- originating subscribers pursuant to the tariff schedules set forth by the call-originating service providers, and revenues or any uncollectible accounts from such tariffs shall go to the call-originating service providers;

tariffs schedules for the local telephone network subscribers using domestic long distance telephone services shall be set by the domestic long distance telephone services provider and tariffs shall be collected from the local telephone network subscribers using domestic long distance telephone services. Revenues or any uncollectible accounts from such tariffs shall go to the domestic long distance telephone services providers; and

tariffs schedules for the local telephone network subscribers using international long distance telephone services shall be set by the international long distance telephone services provider and collected from the local telephone network subscribers using international long distance telephone services. Revenues or any uncollectible accounts from such tariffs shall go to the international long distance telephone service providers.

tariffs schedules for communications between satellite mobile networks and between satellite mobile networks and fixed-line communications networks or mobile communications networks shall both be set by the call-originating service providers. Revenues or any uncollectible accounts from such the tariffs shall go to the call-originating service providers.

Tariffs schedules for communications between the E. 164 VoIP networks provided by the Type I service providers and mobile telecommunications networks, or local telephone networks, or satellite mobile networks shall be set by the call-originating service providers. Revenues or any uncollectible accounts from such tariffs shall go to the call-originating service providers.

Bottleneck Facilities

Under the Telecommunications Act, when a Type I service provider cannot construct bottleneck facilities within a reasonable period of time or substitute those facilities with other available technologies, it may request for co-location on a fee basis from the owner of the facilities located at the bottleneck of the relevant telecommunications network. The owner of the facilities so requested may not reject these requests without due cause. The NCC has the authority to prescribe facilities as bottleneck facilities, and has prescribed bridges, tunnels, lead-in tubes and telecommunications chambers located within buildings and horizontal and vertical telecommunications cables and lines as bottleneck facilities in relation to fixed-line telecommunications networks. The NCC, in an announcement on December 21, 2006, has defined local loop facilities as the bottleneck of the telecommunications network and amended the Administrative Rules for Network Interconnection Between Telecommunication Service Providers in April 2007, providing that we, as a Type I service provider, can only charge other local telephone service providers at cost for local loop services. The rental tariff is derived from a cost basis and must be approved by the NCC each year.

Spectrum Allocation

The Ministry of Transportation and Communications is responsible for allocating all telecommunications related frequencies primarily according to the standards set by the International Telecommunications Union. The NCC is responsible for the licensing of operators to use these frequencies. The 900 MHz and 1,800 MHz frequency bands have been allocated for 2G mobile services and the licenses will be expired in June 2017. A total of 40 MHz of FDD spectrum around the 850 MHz frequency band and a total of 110 MHz of FDD spectrum and 20 MHz of TDD spectrum around the 2 GHz band have been allocated for 3G mobile services.

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The Executive Yuan announced in September 2012 to open up the 4G/mobile broadband licenses, and the NCC will complete the auction process for the 135MHz paired FDD spectrum over 700 MHz, 900 MHz, and 1800MHz frequency bands by December 2013.

Provision of Universal Services

Under the Telecommunications Act, a Type I service provider may be required by the NCC, previously the Ministry of Transportation and Communications, to provide universal telecommunications services in remote or unprofitable areas. These services include voice communication services, such as public phones, and data communication services, such as internet provision for libraries and public primary and secondary schools. All Type I service providers and certain Type II service providers designated by the NCC, previously the Ministry of Transportation and Communications, will be required to contribute a fixed portion of their annual revenues to a universal services fund. Such a fund will be used to compensate for any losses, bad debts and management fees incurred by the relevant Type I service provider in providing the universal services. All providers of universal services cannot refuse any request for service, unless for legitimate reasons, and cannot charge more than the predetermined tariffs.

Equal Access

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

Number Portability

According to the Telecommunications Act and the Administration Rules Governing Number Portability, Type I service providers shall provide number portability service which enables customers to retain their existing local and toll free fixed-line telephone numbers or mobile phone numbers when they switch from the original Type I service provider to other Type I service provider. Meanwhile, Type I service providers shall mutually grant each other number portability services on a reciprocal basis, and shall conform in accordance with the principle of impartiality and reasonableness, and shall not be discriminatory.

Under the regulation, we are required to provide number portability service for fixed-line customers in Taipei City, New Taipei City, Keelung City, Taichung City, Kaohsiung City and other areas where there are two or above fixed-line service providers. We have also provided number portability service for mobile communication customers since October 15, 2005. Pursuant to the regulation, we shall compile and submit related information of number portability for the previous six months to NCC by January 10 and July 10 of each year.

Local Loop Unbundling

In December 2006, the NCC defined the local loop as facilities at the bottleneck of telecommunications networks in accordance with the Regulations Governing Fixed Network Telecommunications Businesses. The NCC requires us to unbundle the local loops and allow other telecommunications operators to use these connections. The local loop or last mile connections are the physical wire connections between the telephone exchange s central office to the customer s premises usually owned by the incumbent telephone company. The NCC further amended the Administrative Rules for Network Interconnection between Telecommunication Service Providers in April 2007 which provides that we can only charge other local telephone service providers at cost for local loop services instead of on the basis of commercial negotiations.

Co-location

We have been declared by the former competent authority NCC as a dominant Type I service provider for fixed-line and mobile services. According to the Telecommunication Act, the Regulations Governing Fixed Network Telecommunications Businesses and the Administrative Rules for Network Interconnection between Telecommunication Service Providers, if any other service provider requests for co-location, we must negotiate with them, unless otherwise provided by laws or regulations. As of the end of 2012, we are currently co-locating 27 POI sites and two cable stations with other Type I fixed-line service providers and 10 POI sites with other Type I mobile service providers.

Ownership Limitations

The laws of the Republic of China limit foreign ownership of our common shares. Prior to March 1, 2006, the Ministry of Transportation and Communications, as the competent authority under the Telecommunications Act, had the power to prescribe the limits on foreign ownership of our common shares. After the formation of the NCC on March 1, 2006, the NCC replaced the Ministry of Transportation and Communications as the competent authority under the Telecommunications Act pursuant to the Organization Law. On July 18, 2006, the Ministry of Transportation and Communications and the NCC reached an agreement where the Ministry of Transportation and Communications will have the authority to adjust foreign ownership limits only after negotiations with the NCC. On June 14, 2007, we applied to both the NCC and the Ministry of Transportation and Communications, asking for an increase in direct and indirect foreign ownership cap of our common shares. After consultation with the NCC, the Ministry of Transportation and Communications raised our foreign ownership cap of direct and indirect shareholdings from 49% to 55%. Our foreign ownership limitation of total direct shareholdings remained at 49%.

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

Fair Trade Act

The requirements and restrictions under the Telecommunication Act regarding price control, IP peering, equal access and accounting separation regulates certain competitive activities among telecommunication industries and aims to reduce the occurrence of anti-competition activities.

By comparison to the Telecommunications Act, the Fair Trade Act, or the FTA, plays a more comprehensive role in regulating all matters relating to competition between enterprises. The Fair Trade Act seeks to deter and prevent anti-competitive conduct by granting the Fair Trade Commission s powers to investigate and to impose penalties.

The Fair Trade Act is administered and enforced by the Fair Trade Commission, or the FTC, which has independent administration rights granted to it under the Fair Trade Act and is empowered to impose disciplinary actions for fair trade matters. The Fair Trade Commission may initiate an investigation either on its own account in accordance with its discretion granted by the Fair Trade Act or upon receipt of a complaint.

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Regulation on Telecommunication Enterprise with Monopoly Status

The term monopoly used in the FTA refers to the circumstance where an enterprise conducts its business operation in a relevant market without facing any competition or where an enterprise is able to dominate the relevant market and block competition in the market. If there are two or more enterprises within the same market that do not engage in any price competition with each other, the whole group of non-competing enterprises should be deemed as a single monopoly enterprise in the market.

According to the FTA, an enterprise or a group of enterprises will not be considered as monopolistic enterprise(s) if none of the following circumstances exists:

- the market share of the enterprise in a relevant market reaches one-half of the market;
- the combined market share of two enterprises in a relevant market reaches two-thirds of the market; and
- the combined market share of three enterprises in a relevant market reaches three-fourths of the market.

If the market share of any respective enterprise does not reach one-tenth of the relevant market or if the amount of the enterprise s total sales in the preceding fiscal year is less than one billion NT dollars, such enterprise shall not be considered as a monopolistic enterprise in the relevant market. Notwithstanding the above, the FTC has the ultimate discretion to consider an enterprise as a monopolistic enterprise upon any other events evidencing such enterprise s capability to affect the supply and demand in relevant market or eliminate competition.

Under the FTA, any enterprise with monopoly status is prohibited from engaging in any of the following activities:

- directly or indirectly, by using any unfair method to prevent any other enterprises from competing;
- improperly set, maintain or change the price for goods or the remuneration for services;
- forcing the enterprise s trading counterpart to give preferential treatment without justification; or
- abusing its market power.

According to the FTC s Explanation on Regulations Governing Telecommunication Industry, a telecommunication enterprise with monopoly status is likely to be involved with the following activities regulated by the FTA: conducting predatory pricing, price squeezing, cross-subsidies, price discrimination, blocking access to essential facilities, entering into long-term agreements to restrict the ability to change counterparties.

Regulations on Combination Between Telecommunication Enterprises

The term merger used in the FTA refers to any of the following circumstances:

- where an enterprise and another enterprise are merged into one;
- where any enterprise holds or acquires more than one-thirds of total voting shares or capital of another enterprise;

where any enterprise is assigned by or leases from another enterprise the whole or the major part of the business or properties of such other enterprise;

where any enterprise operates jointly with another enterprise on a regular basis or is entrusted by another enterprise to operate the latter s business; or

where any enterprise directly or indirectly controls the business operation or the appointment or discharge of personnel of another enterprise.

If any merger between or among multiple enterprises falls within any of the following circumstances, a prior approval granted by the FTC shall be required:

as a result of the merger, the enterprise will own at least one-third of the total market share;

there is any enterprise involved with the merger has one fourth of the market share; or

the sales amount for the preceding fiscal year of one of the enterprises involved with the merger exceeds the threshold amount publicly announced by the FTC from time to time.

Once the telecommunication enterprise files the merger application with the FTC, the FTC will evaluate the pros and cons of the merger by weighing the potential economic efficiency against the disadvantage of reduced competition. If the FTC finds the potential economic efficiency generated from the merger should be able to offset the disadvantage of reduced competition caused, the FTC will grant the approval for the merger.

Regulations on Concerted Action (Cartel) in Telecommunication Industry

The term concerted action (cartel) as used in the FTA means the conduct of any enterprise, by means of contract, agreement or any other form of mutual understanding, with any other competing enterprise, to jointly determine the price of goods or services, or to limit the terms of quantity, technology, products, facilities, trading counterparts, or trading territory with respect to such goods and services, and thereby to restrict each other s business activities. Notwithstanding the above, the term concerted action as used in the FTA is limited to any horizontal concerted action at the same production and/or marketing stage that would affect the market function of production, trade in goods, or supply and demand of services. Under the FTA, the enterprises are prohibited from engaging in any concerted actions unless the FTC holds the concerted action may be beneficial to overall economy and public interest.

According to the FTC s Explanation on Regulations Governing Telecommunication Industry, a telecommunication enterprise may be able to involve with the following concerted actions: entering into common pricing agreement, restriction of output and market segregation, concerted refusal to deal, or entering into agreement for exchange of information.

Regulations on Unfair Competition in Telecommunication Industry

The FTA prohibits any enterprise from conducting any of the following activities that may restrict competition or impede fair competition:

forcing another enterprise to discontinue supply, purchase or other business transactions with a particular enterprise for the purpose of injuring such particular enterprise;

treating another enterprise discriminatively without justification;

forcing the trading counterpart(s) of its competitor(s) to do business with itself by way of coercion, inducement with interest, or other improper means;

forcing another enterprise to refrain from competing in price, or to take part in a merger or a concerted action by coercion, inducement with interest, or other improper methods;

acquiring undisclosed information of another enterprise regarding the production and sales, information concerning trading counterparts or other technology related secret by way of coercion, inducement with interest, or other improper means; or

setting improper restrictions on its trading counterparts business activity as the condition to reach business engagement.

According to the FTC s Explanation on Regulations Governing Telecommunication Industry, the telecommunication enterprise may be involved with the following activities that may restrict competition or impede fair competition: conducting vertical trading restraint, boycott, discrimination, improper sales discount, sales with gift or lottery or tie-in sales.

Regulations on the Representations or Symbol Used by Telecommunication Enterprise on Goods or in Advertisement

The FTA prohibits any enterprise from making or using false or misleading representations or symbol as to price, quantity, quality, content, production process, production date, valid period, method of use, purpose of use, place of origin, manufacturer, place of manufacturing, processor, or place of processing on goods or in advertisements, or in any other way making known to the public.

Other Regulations

In addition to the competitive activities expressly regulated by the FTA, the enterprise shall further be prohibited from conducting any fraudulent activity or significantly unfair activity that may impact the trade order.

The FTC may order any enterprise that violates any of the provisions of the FTA to cease therefrom, rectify its conduct or take necessary corrective action within the time prescribed in the order; in addition, the FTC may assess upon such enterprise an administrative fine of not less than NT$50,000 nor more than NT$25,000,000. Should such enterprise fails to cease therefrom, rectify the conduct or take any necessary corrective action after the lapse of the prescribed period, the FTC may continue to order such enterprise to cease therefrom, rectify the conduct or take any necessary corrective action within the time prescribed in the order, and each time may successively assess thereupon an administrative fine of not less than NT$100,000 nor more than NT$50,000,000 until its ceasing therefrom, rectifying its conduct or taking the necessary corrective action.

If the FTC finds an enterprise liable for violation of regulations governing monopoly or concerted action (cartel), the FTC could impose a monetary fine of up to 10% of the total sales of the enterprise in the preceding fiscal year.

Administrative Fee Law

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

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

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Personal Data Protection

On May 26, 2010, the President of the Republic of China announced the amendment of the Personal Information Protection Act, or PIPA, which replaced the former Computer-Processed Personal Data Protection Act, or CPPDPA, and became fully effective on October 1, 2012, except for its Articles 6 and 54 that await further determination by the Executive Yuan. Under the PIPA, every individuals or governmental or non-governmental agencies, including us, should be subject to certain requirements and restrictions for collecting, processing or using personal data. The definition of personal data is extended to cover a broad scope, including name, birthday, ID, special features, fingerprints, marriage status, family, education, occupation, medical records, medical history, generic information, sex life, health examination report, criminal records, contact information, financial status, social activities, and any other data which is sufficient to directly or indirectly identify a specific person. If we fail to comply with the PIPA, we may be subject to serious punishment for civil claims, criminal offenses and administrative liabilities: the ceiling of the aggregate compensation amount for damages payable in a single case will be up to NT$200 million or the actual value of loss arising from our violation provided the amount of actual value of such loss is higher than NT$200 million; the defendant may be subject to an imprisonment of up to five years; and the penalty for administrative liabilities will be up to NT$500,000 for each violation, and may be imposed consecutively if such violation continues.

Statute of Chunghwa Telecom Co., Ltd.

The Executive Yuan, on April 27, 2012, proposed a motion for the abolishment of the Statute of Chunghwa Telecom Co., Ltd. for legislative approval. We cannot determine when this motion will be approved by the Legislative Yuan. Under Republic of China law, the Statute of Chunghwa Telecom Co., Ltd will continue in effect until the Legislative Yuan formally approves the motion and the President of the Republic of China pronounces the abolishment of the law.

Approval of Ministry of Transportation and Communications

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

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

Employee Subscription Rights for New Issues of Our Common Shares

In accordance with the Statute of Chunghwa Telecom Co., Ltd., our employees have rights to subscribe for not more than 10% of a new issuance of our common shares in accordance with subscription rules which were to be announced by the Ministry of Transportation and Communications. However, no such rules were ever announced. In addition, under the Republic of China Company Act, unless exempted by the relevant government authorities, a Republic of China company must give its employees pre-emptive rights to subscribe for between 10-15% of any new issue of shares by us. The pre-emptive subscription rights do not apply to issuance of restricted shares by a public company to its employees.

C. Organizational Structure

Set forth below is a diagram indicating our organization structure as of March 31, 2013.

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D. Property, Plant and Equipment

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

ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

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

For the convenience of readers, NT dollar amounts used in this section for, and as of, the year ended December 31, 2012 have been translated into U.S. dollar amounts using US$1.00=NT$29.05, set forth in the statistical release of the Federal Reserve Board on December 31, 2012. The U.S. dollar translation appears in parentheses next to the relevant NT dollar amount.

Overview

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

- changes in our revenue composition and sources of revenue growth;

- tariff adjustments;

- capital expenditures as a result of technological improvements and changes in our business;

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provisions for pension payments to our employees; and

taxation.

Each of these developments is discussed below.

Changes in our revenue composition and sources of revenue growth

Our domestic fixed communications business revenues are derived primarily from the provision of local, domestic long distance, broadband access, leased line service, MOD, domestic data services and domestic other services including information and communication technologies, cloud services, corporate solution services, billing handling services and the leasing of real estate properties. In addition, we also derive fixed-line revenues from providing interconnection services to other carriers. Our revenues from mobile communications business are principally derived from the provision of mobile services, sales of mobile handsets and data cards and mobile other services. Our revenues from internet business are generated principally from HiNet internet service, internet VAS, data communication services, internet data center, and internet other services including information and communication technologies and cloud services. Our revenues from international fixed communications business derived primarily from international long distance, international leased line, international data services, satellite services, and international other services. Our other revenues are principally derived from non-telecom services.

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

	Year ended December 31,		
	2010	**2011**	**2012**
Revenues:			
Domestic fixed communications business	34.9%	36.5%	34.3%
Mobile communications business	44.0	42.8	45.8
Internet business	12.1	11.4	11.2
International fixed communications business	7.7	7.0	7.0
Others	1.3	2.3	1.7
Total	100.0%	100.0%	100.0%

Our domestic fixed communications business has been an important source of revenue over the last three years. We derive domestic fixed communications from the provision of ADSL and FTTx access services that provides customers with data access lines. The percentage of total revenues derived from domestic fixed communication increased in 2011 was mainly due to the change in policy for collecting the tariffs for fixed-to-mobile calls from mobile service providers to fixed communications service providers since January 1, 2011, which gave our fixed communications business the right to set and collect the tariffs for fixed-line-to-mobile phone calls. The percentage of total revenues derived from domestic fixed communication decreased in 2012 was mainly due to tariff reductions for ADSL and domestic long distance call services and the decline of local call service revenue because of mobile and VoIP substitution. We believe that domestic fixed communications business will continue to generate a significant portion of our revenues.

Revenues from our mobile communications business made a major contribution to our revenues over the last three years. While the change in policy for collecting the tariffs for fixed-to-mobile calls has caused a decline in our mobile communications business revenues, we have experienced a significant increase in revenues generated by our mobile value-added services due to increased smart phone and mobile internet use by our subscribers. As a result, we believe that our mobile communications business will continue to generate a significant portion of our revenues.

Our internet business was another important source of revenues over the last three years. We derived internet business revenues from the provision of HiNet Internet service and Internet value-added services. The percentage of revenues from internet services within total revenues decreased in 2012 compared to 2011, mainly due to the tariff reduction in internet services along with the ADSL tariff reduction.

Our international fixed communications business was also an important source of our revenues over the last three years. We derived our international fixed communications revenues mainly from international long distance telephone services, international leased line services and international data services. The revenues from our international fixed communications business as a percentage of our total revenues remained flat from 2011 to 2012, while international long distance telephone services revenue continued to decline due to VoIP substitution.

Our other revenues decreased from 2011 to 2012 primarily due to lower property sales by our subsidiary, Light Era Development Co., Ltd., in 2012 compared to 2011.

Tariff adjustments

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

The NCC passed a resolution on December 21, 2006 adopting a price reduction plan requiring the continuous reduction in telecommunication tariffs over three years. Minimum reductions of 4.88% for fixed-line to mobile call tariffs, 4.88% for the tariffs of our highest monthly rate plan, 4.88% for mobile prepaid calling card tariffs and 5.35% for ADSL tariffs must be made each year. The price reduction plan also required us to stop collecting a NT$5.0 monthly maintenance fee from our fixed-line customers who have paid at least 20 years worth of tariffs and customers who chose self-maintenance starting January 1, 2008 and a NT$70.0 fixed-line basic charge from our ADSL customers who only use data services. On January 29, 2010, the NCC announced a new tariff reduction plan starting on April 1, 2010 to March 31, 2013. The percentage of decrease set by NCC was DCPI- 4.816% for IP Peering fees, domestic leased-line fees, ADSL access fees and long distance tariffs, and DCPI-5.00% for fees for mobile calls to local fixed-lines and other networks and domestic mobile SMS, where DCPI is the year-over-year change of the consumer price index of previous year released by the Directorate-General of Budget, Accounting and Statistics of the Executive Yuan. The DCPI for 2010 that was used for the tariff reduction starting from April 1, 2011 was 0.96%; the DCPI for 2011 that was used for the tariff reduction starting from April 1, 2012 was 1.42%; and the DCPI for 2012 that was used for the tariff reduction starting from April 1, 2013 was 1.93%. On February 7, 2013, the NCC announced a new plan for tariff reductions in wholesale tariffs for IP peering and domestic leased line services, and in monthly fees for fixed-line broadband services (excluding fiber-to-the-home, or FTTH, and fiber-to-the-building, or FTTB) over a period of four years starting on April 1, 2013, which are subject to a reduction by DCPI -5.1749%. While mobile tariffs will not be regulated in this round, according to the revised Administrative Rules for Network Interconnection, the mobile interconnection fees should be reduced from the current NT$2.15 per minute to NT$1.15 per minute, over the period of four years starting from January 5, 2013. In addition, each operator was required by the NCC to submit a mobile voice service tariff reduction plan along with the interconnection rate reduction, and the new mobile voice service tariffs became effective on April 1, 2013.

On January 1, 2011, we implemented the NCC s change in policy for collecting the tariffs of fixed-line-to-mobile calls from mobile service providers to fixed communications service providers. As a result, our fixed communications business now has the right to set and collect the tariffs for fixed-line-to-mobile phone calls.

On June 22, 2011, we implemented a discounted tariff along with broadband speed upgrade for our broadband service, under which we provided a 30% or more discount to subscribers of 20 Mbps, 50 Mbps or 100 Mbps broadband access services. We further reduced our ADSL tariffs by approximately 20% starting from 2012 in order to attract more broadband customers. In April 2013, we implemented another discounted tariff for our ADSL and fiber broadband service.

In addition, in 2011, there were complaints from the general public regarding our mobile data network congestion. To address the situation, we adopted measures such as offering a 20% discount of the mobile data monthly fees from August 2011 to the end of 2012 for customers whose monthly data usage volume was less than one gigabyte.

As requested by the Legislative Yuan and NCC, we implemented a discounted tariff for telecommunication services from Kinmen, Matsu and Penghu Islands to Taiwan in April 1, 2011. We further applied one single tariff to all the telecommunication services for the entire country since January 2012.

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

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

In recent years, we have focused on modernizing and upgrading our mobile services network and on developing our FTTx network, which enables transmission of digital information at a high bandwidth over fiber loops. In particular, we have enhanced our telecommunications services through:

- the introduction of a IP-based exchange system in our long distance telephone network;
- the implementation of a network modernization program, including a gradual transfer from our public switched telephone network to a system based on internet protocol, to remain at the forefront of new technologies;
- the development and deployment of Green IDC for meeting the new demands of cloud computing services;
- the deployment of a high-capacity long-haul reconfigurable optical add drop multiplexing system and a nationwide internet protocol backbone network with thousands of Gbps switching routers for internet and managed IP services; and
- the expansion and upgrade of our mobile services network as well as WiFi/Femtocell to improve indoor and outdoor 3G mobile network coverage and transmission speed for mobile internet.

As a result, we made aggregate capital expenditures of NT$140.4 billion over the period from January 1, 2008 to December 31, 2012.

Our long-term goal is to optimize our capital expenditures by focusing on investing in innovative products and services with attractive return profiles. We evaluate our investment opportunities by benchmarking them against internal return requirements. We are upgrading our public switched telephone network to a next-generation network, which will have more capacity, greater upgrade flexibility, and increased operational efficiencies. We have also devoted resources toward the effective upgrade of our 3G mobile network to 3.5G and HSPA+/Dual cell HSPA+ and the continuing build-out of our FTTx infrastructure. In addition, we are planning to deploy green internet Data Centers and service delivery network for the innovative services, such as cloud computing, fixed mobile convergence services and four-screen digital convergence services.

Provisions for pension payments to our employees

Personnel expenses constitute a significant portion of our operating costs and expenses. In 2010, 2011 and 2012, personnel expenses represented 30.4%, 27.6% and 25.9% of our total operating costs and expenses, respectively, and pension costs represented 2.0%, 1.8% and 1.8% of our total operating costs and expenses, respectively. The table below sets forth information regarding our personnel expenses and as a percentage of our total operating costs and expenses for the periods indicated.

	For the year ended December 31,					
	2010		2011		2012	
	(in billions of NT$, except percentages)					
Personnel expenses:						
Salaries	22.9	15.8%	23.6	14.6%	24.3	14.2%
Insurance	1.9	1.3	2.0	1.2	2.3	1.3
Pension	2.9	2.0	3.0	1.8	3.1	1.8
Other	16.4	11.3	16.2	10.0	14.7	8.6

Total personnel expenses	44.1	30.4%	44.8	27.6%	44.4	25.9%
Total operating costs and expenses	145.0	100.0%	162.4	100.0%	171.2	100.0%

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At the time of our privatization, we settled all of our then existing defined benefit pension obligations in full. After completing our privatization on August 12, 2005, all of our continuing employees were deemed to have commenced employment as of August 12, 2005 for seniority purposes under our pension plans in effect after privatization. Under applicable Republic of China regulations, upon our privatization, the Ministry of Transportation and Communications assumed the obligation to make annuity payments to all of our employees that retired before our privatization.

Taxation

The income tax rate for profit-seeking enterprises is 17% in the Republic of China. We benefit from tax incentives, including tax credits of up to 15% of some of our research and development expenses in accordance with the Statute for Innovating Industries. We also qualify for tax benefits at a rate of 5% to 15% of our investment amount for qualified equipment and technology under the Statute for Upgrading Industries. However, due to the expiration of the Statute for Upgrading Industries at the end of 2009, we will no longer receive tax credits for new investments in automation, employee training expenditures incurred, and equipment and technology purchased after January 2010. As a result, though our effective tax rate was 15.8%, 15.2% and 16.1% in 2010, 2011 and 2012, respectively, our effective tax rate may rise in the future because of fewer tax incentives.

In 1997, the Income Tax Law of the Republic of China was amended to integrate corporate income tax and stockholder dividend tax to eliminate the double taxation effect for resident stockholders of Taiwan companies. Under the amendment, all retained earnings generated from January 1, 1998 and not distributed to stockholders as dividends in the following year are assessed with a 10% retained earnings tax. See Item 10. Additional Information E. Taxation Republic of China Taxation Dividends . This has not had an impact on our financial results of operations because of our high dividend payout policy.

Critical Accounting Policies

Summarized below are our accounting policies that we believe are both important to the portrayal of our financial results and involve the need for management to make estimates about the effect of matters that are uncertain in nature. Actual results may differ from these estimates, judgments and assumptions. Certain accounting policies are particularly critical because of their significance to our reported financial results and the possibility that future events may differ significantly from the conditions and assumptions underlying the estimates used and judgments made by our management in preparing our financial statements. The following discussion should be read in conjunction with the consolidated financial statements and related notes, which are included in this annual report.

Revenue Recognition

We recognize revenues when we have 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 collectability is reasonably assured. We measure revenues at the fair value of the consideration received or receivable and represents amounts agreed between us and the customers for goods sold in the normal course of business, net of sales discounts and volume rebates. The costs of providing services are recognized as incurred.

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 seconds or minutes of traffic processed when the services are provided in accordance with contract terms.

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We recognize other revenues as follows: (i) one-time subscriber connection fees (on fixed-line services) are deferred and recognized over the average expected customer service periods, (ii) monthly fees (on fixed-line services, mobile and internet and data services) are accrued every month, and (iii) prepaid services (fixed-line, mobile and internet and data services) are recognized as income based upon actual usage by customers or when the right to use those services expires. Where we enter 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. Relative fair values are based on the selling prices of 3G data cards and handsets sold on a standalone basis and the monthly fees on the subscription contracts.

Where we sell products to third-party cellular phone stores we record the direct sale of the products, typically handsets, as gross revenue when we are the primary obligor in the arrangement and when title is passed and the products are accepted by the stores.

Impairment of Accounts Receivable

We maintain allowances for doubtful accounts for estimated losses that result from the inability of our customers to make required payments before January 1, 2011. We assess the probability of collections of accounts receivable by examining the aging analysis of the outstanding receivables and assessing the value of the collateral provided by customers.

On January 1, 2011, we adopted the third-time revised Statement of Financial Accounting Standards No. 34, Financial Instruments: Recognition and Measurement . One of the main revisions is that the impairment of receivables originated by us should be covered by 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.

We implemented new measures starting from 2010 which have improved the collectability of our accounts receivable. These new procedures, which include enhanced credit assessments, strengthened overall risk management and improvements in bill collection practices, have reduced our exposure to uncollected receivables. These improvements enabled us to refine our estimates, which led to the reversal in the allowance for bad debt.

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.

Estimated Useful Lives of Long-Lived Assets

A significant portion of our total assets consists of long-lived assets, primarily property, plant and equipment and definite-lived intangibles. We estimate the useful lives of property, plant and equipment and other long-lived assets with finite lives in order to determine the period of time over which depreciation and amortization expense should be recorded. The useful lives are estimated at the time assets are acquired and are based on historical experience with similar assets as well as the anticipated technological evolution or other environmental changes. If technological changes were to occur more rapidly than anticipated or in a different form than anticipated, the useful lives assigned to these assets may need to be shortened, resulting in the recognition of increased depreciation and amortization in the relevant periods. Alternatively, technological obsolescence could result in a write-down in the value of the assets to reflect impairment. We review these types of assets for impairment quarterly, or when events or circumstances indicate that the carrying amount may not be recoverable over the remaining life of an asset. In assessing impairments, we use estimated cash flows that take into account management s estimates of future operations. We did not have a significant impairment loss of long-lived assets in 2011, but had NT$66 million impairment loss in 2010. In 2012, we determined that partial land and telecommunication equipment were impaired and recognized an impairment loss of NT$1,505 million (US$51.8 million). In 2012, we also recognized impairment losses of NT$4.8 million (US$0.2 million), NT$35 million (US$1.2 million) and NT$20 million (US$0.7 million) for intangible assets, idle assets and other assets, respectively.

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Investments in Unconsolidated Companies

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

We assess the impairment of investments accounted for using the equity method whenever triggering events or changes in circumstances indicate that an investment may be impaired and carrying value may not be recoverable. We measure the impairment based on the projected future cash flow of the investees, the underlying assumptions for which had been formulated by such investees internal management team, taking into account sales growth and capacity utilization.

The process of assessing whether a particular cost method investment s net realizable value is less than its carrying cost requires a significant amount of judgment. We periodically evaluate these long-term investments based on quoted market prices, if available, the financial condition of the investee company, economic conditions in the industry and our intent and ability to hold the investment for a long period of time. If quoted market prices are not available, we estimate the fair value using the net asset values as well as the financial condition of the investee company. This information may be based on information that we request from the investee companies and may not be subject to the same disclosure and audit requirements as required of non-foreign private issuers, and as such, the reliability and accuracy of the information may vary. If we deem the fair value of an investment to be less than the book value based on the above factors, and the decline in value is deemed to be other than temporary, we record the difference as impairment in the period of occurrence. In 2012, we recognized impairment losses of NT$176 million (US$6.1 million) for the investments classified as financial assets carried at cost due to adverse changes in industry conditions and operating performance that was below expectations. Note 14 to our consolidated financial statements included elsewhere in this annual report sets forth the individual impairment loss of each investee.

Valuation of long-lived assets and intangible assets

We assess the impairment of long-lived assets and intangible assets whenever triggering events or changes in circumstances indicate that the asset may be impaired and carrying value may not be recoverable. Indications we consider important which could trigger an impairment review include, but are not limited to, the following:

- External sources of information:
  - during the period, an asset s market value has declined significantly more than would be expected as a result of the passage of time or normal use.
  - significant changes with an adverse effect on the entity have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the entity operates or in the market to which an asset is dedicated.
  - market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset s value in use and decrease the asset s recoverable amount materially.
  - the carrying amount of the net assets of the entity is more than its market capitalization.

Internal sources of information:

evidence is available of obsolescence or physical damage of an asset.

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significant changes with an adverse effect on the entity have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used.

evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.

When an indication of impairment is identified for long-lived assets and intangible assets 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 for business acquisition 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 Benefits

The amounts recognized in our consolidated financial statements related to defined benefit pension are determined on an actuarial basis that utilizes several different assumptions in the calculation of such amounts. Significant assumptions used in determining our pension benefits are the discount rate, the expected long-term rate of return on plan assets, the rate of increase in compensation levels, and the average remaining years of service for employees.

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

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.

Accounting for Income Taxes

Deferred income taxes represent the effect of temporary differences between the amounts of assets and liabilities recognized for financial reporting purposes and the amounts recognized for income tax purposes. We measure deferred tax assets and liabilities using statutory tax rates that, if changed, would result in either an increase or a decrease in the provision for income taxes in the period of change.

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

We had a valuation allowance of NT$109 million (US$3.8 million) on our deferred tax asset balance as of December 31, 2012. We do not have a full valuation allowance on the deferred tax asset, as we believe these benefits will be partially realizable based on our projection of future operating income. If we experience a significant decrease in our future operating income, our ability to realize the deferred tax assets could be negatively impacted, and thus an increase in the valuation allowance might be required.

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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. Under ROC GAAP, income taxes of 10% on undistributed earnings are recorded in the year of stockholders approval which is the year subsequent to the year the earnings are generated. Under U.S. 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.

Effective from January 1, 2007, we adopted a guidance prescribing the 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 under U.S. GAAP. This guidance also provides guidance on derecognition, classification, interest and penalties, disclosure and transition. The evaluation of a tax position in accordance with this 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 estimates. The adoption of this guidance did not have a material impact on our results of operation, financial position and cash flows. We did not identify significant unrecognized tax benefits for each of the years ended December 31, 2010, 2011 and 2012. It is highly unlikely that we will incur any interests or penalties related to potential underpaid income tax expenses.

Our Financial Reporting Obligations

Our ongoing financial reporting in our Form 20-F annual reports and interim financial reporting furnished to the SEC on Form 6-K had been based on U.S. GAAP through fiscal year 2007. Beginning with our first quarter interim financial report furnished on Form 6-K and our Form 20-F annual report for fiscal year 2008, we prepared our financial statements under ROC GAAP, with reconciliations to U.S. GAAP.

A. Operating Results

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

	For the year ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
	(in billions)			
Revenues:				
Domestic Fixed Communications	70.7	79.4	75.5	2.6
Mobile communications	89.0	93.0	100.8	3.5
Internet	24.5	24.8	24.8	0.9
International fixed communications	15.5	15.2	15.3	0.5
Others	2.7	5.1	3.7	0.1
Net revenues	202.4	217.5	220.1	7.6
Operating costs and expenses:				
Operating costs	115.3	131.5	141.2	4.9
Operating expenses:				
Marketing	22.5	23.2	22.3	0.8
General and administrative	4.0	4.2	4.0	0.1
Research and development	3.2	3.5	3.7	0.1
Total operating costs and expenses	145.0	162.4	171.2	5.9
Income from operations	57.4	55.1	48.9	1.7
Other income, net	0.3	1.6		
Income before income tax expense	57.7	56.7	48.9	1.7

Income tax expense	9.1	8.6	7.9	0.3
Consolidated net income	48.6	48.1	41.0	1.4
Attributable to:				
Stockholders of the parent	47.6	47.1	39.9	1.4
Minority interests	1.0	1.0	1.1	

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

	For the year ended December 31, 2010	2011	2012
	(as percentages of total revenues)		
Revenues:			
Domestic fixed communications	34.9%	36.5%	34.3%
Mobile communications	44.0	42.8	45.8
Internet	12.1	11.4	11.2
International fixed communications	7.7	7.0	7.0
Others	1.3	2.3	1.7
Total revenues	100.0%	100.0%	100.0%
Operating costs and expenses:			
Operating costs	57.0%	60.5%	64.2%
Operating expenses:			
Marketing	11.1	10.7	10.1
General and administrative	2.0	1.9	1.8
Research and development	1.6	1.6	1.7
Total operating costs and expenses	71.7	74.7	77.8
Income from operations	28.3	25.3	22.2
Other income, net	0.2	0.8	
Income before income tax expense	28.5	26.1	22.2
Income tax expense	4.5	4.0	3.6
Consolidated net income	24.0%	22.1%	18.6%
Attributable to:			
Stockholders of the parent	23.5%	21.6%	18.1%
Minority interests	0.5%	0.5%	0.5%

Each of our operating segments is managed separately because each represents a strategic business unit that serves a different market. We measure our segment performances mainly based on revenues and income before tax.

The year ended December 31, 2012 compared with the year ended December 31, 2011

Revenues

Our revenues increased by 1.2% from NT$217.5 billion in 2011 to NT$220.1 billion (US$7.6 billion) in 2012. This increase was primarily due to increase in revenues generated from mobile communications business sector.

Domestic fixed communications

Domestic fixed communications revenues comprised 36.5% and 34.3% of our revenues in 2011 and 2012, respectively. Our domestic fixed-line revenues decreased by 4.9% from NT$79.4 billion in 2011 to NT$75.5 billion (US$2.6 billion) in 2012.

Local telephone services. Our local telephone revenues decreased from NT$41.7 billion in 2011 to NT$40.2 billion (US$1.4 billion) in 2012. This reflects a 7.7% decline in traffic volume from 15.6 billion minutes in 2011 to 14.4 billion minutes in 2012. The decline in traffic volume was primarily due to the traffic migration from fixed-line services to mobile and internet telephone services. We expect this trend to continue as broadband and mobile services become more widely adopted in Taiwan.

Domestic long distance telephone services. Our domestic long distance telephone revenues decreased by 34.9% from NT$5.8 billion in 2011 to NT$3.8 billion (US$0.1 billion) in 2012. This decrease was mainly due to domestic long distance call tariff reduction starting from 2012. The increase in traffic volume was primarily due to the tariff reduction. Our interconnection revenues also decreased primarily because the telecommunications operators construct their own interconnection circuit.

Broadband access. The number of our ADSL customers decreased from 2.1 million in 2011 to 1.8 million in 2012 due to customer migration to our FTTx services. There was an increase in the number of FTTx customers from approximately 2.4 million in 2011 to approximately 2.7 million in 2012. Broadband access revenue decreased from NT$20.4 billion for 2011 to NT$19.2 billion (US$0.7 billion) for 2012 mainly due to the approximate 20% tariff reduction in ADSL starting from 2012, and the NCC s mandated tariff reduction.

Domestic leased line. Our overall leased line tariffs have continued to be adversely affected by competition from other fixed-line operators, as well as the continued migration of domestic leased line customers to broadband services. Domestic leased line revenue decreased from NT$5.7 billion for 2011 to NT$5.4 billion (US$0.2 billion) for 2012.

MOD. Our MOD revenues increased by 36.0% from NT$1.4 billion in 2011 to NT$2.0 billion (US$0.1 billion) in 2012. This increase was due to the increases in the number of subscribers and in the average revenue per user.

Others. Other revenues increased by 14.0% from NT$4.4 billion in 2011 to NT$4.9 billion (US$0.2 billion) in 2012. This increase was mainly due to an increase in corporate solution ICT business and the hot selling of high definition TV.

Mobile communications

Revenues from our mobile communications business segment comprised 42.8% and 45.8% of our revenues in 2011 and 2012, respectively. Revenues from our mobile communications business segment increased by 8.4% from NT$93.0 billion in 2011 to NT$100.8 billion (US$3.5 billion) in 2012. This increase was principally due to the growth of mobile VAS revenue and handset sales revenue offsetting the decline of mobile voice revenue over years. The growth of mobile voice traffic was mainly due to our promotional plans.

Mobile services. Revenues from our mobile services comprised 32.6% and 32.9% of our revenues in 2011 and 2012, respectively. Revenues from our mobile services increased by 2.2% from NT$70.9 billion in 2011 to NT$72.5 billion (US$2.5 billion) in 2012 due to the growth of mobile VAS revenue from NT$15.2 billion in 2011 to NT$20.4 billion (US$0.7 billion) in 2012, which offset the decline of mobile voice revenue.

Sales of mobile handsets and data cards. Revenues from our sales of mobile handsets and data cards comprised 10.1% and 12.8% of our revenues in 2011 and 2012, respectively. Revenues from our sales of mobile handsets and data cards increased by 28.3% from NT$22.0 billion in 2011 to NT$28.2 billion (US$1.0 billion) in 2012. This increase was principally due to the strong sales of mobile smart phones.

Internet

Internet revenues comprised 11.4% and 11.2% of our revenues in 2011 and 2012, respectively. Our revenues attributable to our internet business remained flat at NT$24.8 billion (US$0.9 billion) in 2011 and 2012. The increase in the internet VAS revenue was offset by the tariff reduction for the HiNet ISP service along with the broadband access tariff reduction. As of December 31, 2012, approximately 82.8% of our broadband customers were also HiNet subscribers, using HiNet as their ISP.

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International fixed communications

As a percentage of our revenue, international fixed communications revenues remained flat at 7.0% in 2011 and 2012. Our international fixed communications revenues increased by 0.7% from NT$15.2 billion in 2011 to NT$15.3 billion (US$0.5 billion) in 2012. This increase was mainly due to the increase in revenues from our international leased line services and international data services.

International long distance telephone services. Our international long distance telephone revenues decreased by 2.9% from NT$12.4 billion in 2011 to NT$12.1 billion (US$0.4 billion) in 2012 due to market competition.

International leased line and international data services. Our international leased line and international data revenues increased by 12.1% from NT$2.1 billion in 2011 to NT$2.5 billion (US$0.1 billion) in 2012. The increase was mainly because of the overseas market expansion and the increased demand of multinational corporations.

Others

Other revenues comprised 2.3% and 1.7% of our revenues in 2011 and 2012, respectively. Our other revenues decreased by 27.1% from NT$5.1 billion in 2011 to NT$3.7 billion (US$0.1 billion) in 2012. The decrease was mainly due to lower property sales by our subsidiary, Light Era Development Co., Ltd., in 2012 compared with 2011.

Operating Costs and Expenses

Our operating costs and expenses increased by 5.4% from NT$162.4 billion in 2011 to NT$171.2 billion (US$5.9 billion) in 2012. This increase was primarily due to an increase in costs of handsets sold. As a percentage of revenues, operating costs and expenses increased from 74.7% in 2011 to 77.8% in 2012.

Operating Costs

Operating costs include depreciation and amortization expense, personnel expenses, cost of goods sold, interconnection and service expense, costs of materials and maintenance and spectrum usage and license fees.

Our operating costs increased by 7.4% from NT$131.5 billion in 2011 to NT$141.2 billion (US$4.9 billion) in 2012. This increase was primarily a result of an increase of NT$8.5 billion (US$0.3 billion) in cost of goods sold due to an increase in the sales of smart phones, an increase of NT$0.5 billion (US$0.02 billion) in rental expenses, an increase of NT$0.3 billion (US$0.01 billion) in maintenance and material expenses in order to support our broadband and mobile internet service build-out, an increase of NT0.3 billion (US$0.01 billion) in the electricity expense due to the increase in electricity tariff, and a NT$0.3 billion (US$0.01 billion) increase in ICT costs due to the growth in ICT business. These increases were partially offset by a decrease of NT$0.4 billion (US$0.01 billion) in personnel expenses mainly due to the decrease in amount of bonuses paid.

Marketing

Our marketing expenses, which include personnel expenses, expenses relating to advertising and marketing-related activities and provision for bad debt, decreased by 3.9% from NT$23.2 billion in 2011 to NT$22.3 billion (US$0.8 billion) in 2012. This decrease was primarily a result of a NT$1.5 billion (US$0.05 billion) reversal of bad debts allowance, which was partially offset by an increase of NT$0.5 billion (US$0.02 billion) in expenses relating to personnel and marketing-related activities from our subsidiary, Senao. See Critical Accounting Policies Impairment of Accounts Receivable for a discussion of our policy for bad debts allowance.

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General and administrative

Our general and administrative expenses decreased by 4.8% from NT$4.2 billion in 2011 to NT$4.0 billion (US$0.1 billion) in 2012. This decrease was primarily a result of a NT$0.1 billion (US$0.01 billion) decrease due to deconsolidation of a subsidiary after we lost control over it in June 2011, and a NT$0.1 billion (US$0.01 billion) decrease in bonus.

Research and development

Our research and development expenses increased by 5.7% from NT$3.5 billion in 2011 to NT$3.7 billion (US$0.1 billion) in 2012. This increase was principally a result of an increase in the number of research and development employees we hired in 2012.

Operating Costs and Expenses by Business Segment

	Domestic						
	Fixed Communications	Mobile Communications	Internet	International Fixed Communications	Others	Adjustment	Total
For the year ended December 31, 2012							
Operating costs and expenses	76.4	81.4	19.0	16.2	7.9	(29.7)	171.2
Depreciation and amortization	19.4	8.7	2.7	1.4	0.3		32.5
For the year ended December 31, 2011							
Operating costs and expenses	76.7	72.3	17.2	15.8	8.0	(27.6)	162.4
Depreciation and amortization	20.1	8.3	2.3	1.3	0.3		32.3

Domestic fixed communications

Our domestic fixed communications costs and expenses decreased by 0.4% from NT$76.7 billion in 2011 to NT$76.4 billion (US$2.6 billion) in 2012, primarily due to a NT$0.7 billion (US$0.02 billion) decrease in bonus, which was partially offset by a NT$0.4 billion (US$0.01 billion) increase in corporate solution services and ICT costs.

Mobile communications

Our mobile communications operating costs and expenses increased by 12.6% from NT$72.3 billion in 2011 to NT$81.4 billion (US$2.8 billion) in 2012. This increase was primarily due to an increase of NT$7.6 billion (US$0.3 billion) in cost of handsets sold, and a NT$1.9 billion (US$0.1 billion) increase in leased line and internet access expenses resulting from the increasing leased lines and higher speed rate to support our mobile internet services.

Internet

Our internet operating costs and expenses increased by 10.5% from NT$17.2 billion in 2011 to NT$19.0 billion (US$0.7 billion) in 2012. This increase was primarily due to a NT$0.8 billion (US$0.03 billion) increase in leased line expenses to promote the broadband access speed, a NT$0.4 billion (US$0.01 billion) increase in depreciation and amortization expenses due to increasing cloud computing related facilities, and a NT$0.2 billion (US$0.01 billion) increase in corporate solution services and ICT costs.

International fixed communications

Our international fixed communications costs and expenses increased by 2.5% from NT$15.8 billion in 2011 to NT$16.2 billion (US$0.6 billion) in 2012. The increase was primarily due to an increase of NT$0.5 billion (US$0.02 billion) in settlement payments for international long distance calls.

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Others

The costs and expenses from our other business decreased by 1.3% from NT$8.0 billion in 2011 to NT$7.9 billion (US$0.3 billion) in 2012. The decrease was primarily due to lower property sales by our subsidiary, Light Era Development Co., Ltd., in 2012 compared to 2011, which was partially offset by the increase of ICT costs from our subsidiary, Chunghwa System Integration Co., Ltd.

Income from Operations and Operating Margin

As a result of the foregoing, our income from operations decreased by 11.3% from NT$55.1 billion in 2011 to NT$48.9 billion (US$1.7 billion) in 2012. Our operating margin decreased from 25.3% in 2011 to 22.2% in 2012.

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

	Domestic Fixed Communications	Mobile Communications	Internet	International Fixed Communications (in billions of NT$)	Others	Adjustment	Total
For the year ended December 31, 2012							
Revenues from external customers	75.5	100.8	24.8	15.3	3.7		220.1
Intersegment service revenues	17.0	6.6	2.9	2.2	1.0	(29.7)	
Interest income					0.7		0.7
Other income	0.2	0.2			0.7		1.1
	92.7	107.6	27.7	17.5	6.1	(29.7)	221.9
Segment income before tax	15.0	25.8	8.6	1.3	(1.8)		48.9
For the year ended December 31, 2011							
Revenues from external customers	79.4	93.0	24.8	15.2	5.1		217.5
Intersegment service revenues	15.4	7.0	1.9	2.6	0.7	(27.6)	
Interest income					0.7		0.7
Other income	0.4	0.1		0.1	0.6		1.2
	95.2	100.1	26.7	17.9	7.1	(27.6)	219.4
Segment income before tax	18.5	27.8	9.6	2.0	(1.2)		56.7

As a result of the foregoing, segment income before tax for our domestic fixed communications business decreased by 18.9% from NT$18.5 billion in 2011 to NT$15.0 billion (US$0.5 billion) in 2012; segment income before tax for our mobile communications business decreased by 7.2% from NT$27.8 billion in 2011 to NT$25.8 billion (US$0.9 billion) in 2012; segment income before tax for our internet business decreased by 10.4% from NT$9.6 billion in 2011 to NT$8.6 billion (US$0.3 billion) in 2012; segment income before tax for our international fixed communications business decreased by 35.0% from NT$2.0 billion in 2011 to NT$1.3 billion (US$0.04 billion) in 2012; and segment loss for our others business segment increased by 50.0% from NT$1.2 billion in 2011 to NT$1.8 billion (US$0.1 billion) in 2012.

Other Income, Net

Our other income, net decreased from NT$1.6 billion in 2011 to the net loss NT$17.0 million (US$0.6 million) in 2012. This decrease was primarily due to an increase of impairment loss of NT$1.6 billion (US$0.1 billion) on financial assets, property, plant, and equipment, intangible assets, idle assets and other assets. Please refer to Item 3. Key Information D. Risk Factors for further description. This decrease was also due to the smaller decrease of gain on disposal of property, plant and equipment of NT$0.3 billion (US$10.3 million), which was partially offset by a higher increase in earnings of equity method investees of NT$0.2 billion (US$5.7 million).

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Income Tax

Our income tax was NT$8.6 billion in 2011, compared to NT$7.9 billion (US$0.3 billion) in 2012. Our effective tax rate was 15.2% in 2011 and 16.1% in 2012. The increase of our effective tax rate from 2011 to 2012 was primarily due to fewer tax incentives available under new regulations. We will no longer receive tax credits for new investments in automation, employee training expenditures incurred, and equipment and technology purchased. Please refer to Item 5. Operating and Financial Review and Prospects Taxation for a discussion of the change in tax incentives.

Net Income

As a result of the foregoing, our net income attributable to stockholders of the parent decreased by 15.3% from NT$47.1 billion in 2011 to NT$39.9 billion (US$1.4 billion) in 2012. Our net margin was 21.6% in 2011 and 18.1% in 2012.

The year ended December 31, 2011 compared with the year ended December 31, 2010

Revenues

Our revenues increased by 7.4% from NT$202.4 billion in 2010 to NT$217.5 billion in 2011. This increase was primarily due to increase in revenues generated from domestic fixed communications, mobile communications, and other business sectors.

Domestic fixed communications

Domestic fixed communications revenues comprised 34.9% and 36.5% of our revenues in 2010 and 2011, respectively. Our domestic fixed-line revenues increased by 12.3% from NT$70.7 billion in 2010 to NT$79.4 billion in 2011.

Local telephone services. Our local telephone revenues increased from NT$32.3 billion in 2010 to NT$41.7 billion in 2011. This reflects the shift in policies for collecting the tariffs for fixed-to-mobile calls from mobile service providers to fixed communications service providers since January 1, 2011, which gave our fixed communications business the right to set and collect the tariffs for fixed-line-to-mobile phone calls. Traffic volume increased from 13.7 billion minutes in 2010 to 15.6 billion minutes in 2011. We primarily attribute the increase in traffic volume to the inclusion of fixed-line-to-mobile calls under this category as a result of the NCC s change in policy for collecting the tariffs from fixed-line-to-mobile calls starting from 2011. For the same reason, our local interconnection revenues decreased by NT$1.0 billion from NT$2.4 billion in 2010 to NT$1.4 billion in 2011 because fixed communications service providers received less interconnection charges from mobile service providers.

Domestic long distance telephone services. Our domestic long distance telephone revenues decreased by 12.9% from NT$6.6 billion in 2010 to NT$5.8 billion in 2011. This decrease was mainly due to a decrease in traffic volume from 3.4 billion minutes in 2010 to 3.2 billion minutes in 2011. The decrease in traffic volume was primarily due to the continued traffic migration from fixed-line services to mobile services and VoIP.

Broadband access. The number of our ADSL customers decreased from 2.3 million in 2010 to 2.1 million in 2011 due to customer migration to our FTTx services. There was an increase in the number of FTTx customers from approximately 2.0 million in 2010 to approximately 2.4 million in 2011. Broadband access revenue increased from NT$20.3 billion for 2010 to NT$20.4 billion for 2011.

Domestic leased line. While demand for higher speed leased lines continues to increase, our overall leased line tariffs have continued to be adversely affected by competition from other fixed-line operators, as well as the continued migration of domestic leased line customers to broadband services. Domestic leased line revenue decreased from NT$6.1 billion for 2010 to NT$5.7 billion for 2011.

MOD. Our MOD revenues increased by 31.2% from NT$1.1 billion in 2010 to NT$1.4 billion in 2011. This increase was mainly due to an increase in the number of subscribers.

Others. Other revenues increased by 0.4% from NT$4.3 billion in 2010 to NT$4.4 billion in 2011. This increase was mainly due to an increase in corporate solution ICT business.

Mobile communications

Revenues from our mobile communications business segment comprised 44.0% and 42.8% of our revenues in 2010 and 2011, respectively. Revenues from our mobile communications business segment increased by 4.4 % from NT$89.0 billion in 2010 to NT$93.0 billion in 2011. This increase was principally due to the growth of mobile VAS revenue and handset sales revenue offsetting the decline of mobile voice revenue since 2008. The growth of mobile voice traffic due to the general recovery of the economy in the ROC was partially offset by the mandatory tariff reduction and the impact from the change in policy for collecting the tariffs for fixed-line-to-mobile calls from mobile service providers to fixed communications service providers since January 1, 2011, which gave our fixed communications business the right to set and collect the tariffs for fixed-line-to-mobile phone calls.

Mobile services. Revenues from our mobile services comprised 36.1% and 32.6% of our revenues in 2010 and 2011, respectively. Revenues from our mobile services decreased by 3% from NT$73.1 billion in 2010 to NT$70.9 billion in 2011 due to the decline of mobile voice revenue as a result of the change in policy for collecting the tariffs for fixed-line-to-mobile phone calls from mobile service providers to fixed communications service providers, and the mandatory tariff reduction, which was partially offset by the growth of mobile VAS revenue from NT$11.1 billion in 2010 to NT$15.2 billion in 2011.

Sales of mobile handsets and data cards. Revenues from our sales of mobile handsets and data cards comprised 7.9% and 10.1% of our revenues in 2010 and 2011, respectively. Revenues from our sales of mobile handsets and data cards increased by 38.4% from NT$15.9 billion in 2010 to NT$22.0 billion in 2011. This increase was principally due to the strong sales of mobile smart phones and the general recovery of the economy in the ROC

Internet

Internet revenues comprised 12.1% and 11.4% of our revenues in 2010 and 2011, respectively. Our revenues attributable to our internet business increased by 1.4 % from NT$24.5 billion in 2010 to NT$24.8 billion in 2011. The increase was mainly due to a 3% increase in the number of our total HiNet broadband subscribers from approximately 3.6 million as of December 31, 2010 to approximately 3.7 million as of December 31, 2011. Our HiNet subscribers remained at approximately 4.1 and 4.2 million subscribers as of December 31, 2010 and 2011, respectively. As of December 31, 2011, approximately 82% of our broadband access customers were also HiNet subscribers, using HiNet as their ISP.

International fixed communications

International fixed communications revenues comprised 7.7% and 7.0% of our revenues in 2010 and 2011, respectively. Our international fixed communications revenues decreased by 2% from NT$15.5 billion in 2010 to NT$15.2 billion in 2011. This decrease was mainly due to the decrease in international long distance service revenue as a result of intensified market competition.

International long distance telephone services. Our international long distance telephone revenues decreased by 3.4% from NT$12.9 billion in 2010 to NT$12.4 billion in 2011 because of the decline in traffic volumes as a result of intensified market competition.

International leased line and international data services. Our international leased line and international data revenues increased by 6% from NT$2.0 billion in 2010 to NT$2.1 billion in 2011. The increase was mainly because of the overseas market expansion and the increased demand of multinational corporations.

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Others

Other revenues comprised 1.3% and 2.3% of our revenues in 2010 and 2011, respectively. Our other revenues increased by 90.0% from NT$2.7 billion in 2010 to NT$5.1 billion in 2011. The increase was mainly due to higher property sales by our subsidiary, Light Era Development Co., Ltd.

Operating Costs and Expenses

Our operating costs and expenses increased by 12.0% from NT$145.0 billion in 2010 to NT$162.4 billion in 2011. This increase was primarily due to the higher cost of handsets sold, interconnection costs and transition fees resulting from the change in policy for collecting the tariffs of fixed-line-to-mobile phone calls.

Operating costs

Operating costs include depreciation and amortization expense, personnel expenses, cost of goods sold, interconnection and service expense, costs of materials and maintenance and spectrum usage and license fees.

Our operating costs increased by 14.0% from NT$115.3 billion in 2010 to NT$131.5 billion in 2011. This increase was principally a result of an increase of NT$8.1 billion in cost of goods sold, an increase of NT$7.1 billion in interconnection and service expenses mainly due to the change in policy for collecting the tariffs of fixed-line-to-mobile phone calls, an increase of NT$1.0 billion in maintenance and material expenses due to expansion of broadband facilities, a NT$1.0 billion increase in corporate solution ICT costs due to the increase in revenue. These increases were partially offset by a decrease of NT$1.8 billion in depreciation.

Marketing

Our marketing expenses, which include personnel expenses, expenses relating to advertising and marketing-related activities and provision for bad debt increased by 3.1% from NT$22.5 billion in 2010 to NT$23.2 billion in 2011. This increase was principally a result of a NT$0.3 billion increase in salary expenses due to headcount growth, and NT$0.2 billion in expenses relating to human resource outsourcing services for the sales division.

General and administrative

Our general and administrative expenses increased by 4.2% from NT$4.0 billion in 2010 to NT$4.2 billion in 2011. This increase was principally a result of new business in mobile industry in Mainland China and an increase in personnel expenses mainly due to salary increases, additional employees and bonuses.

Research and development

Our research and development expenses increased by 8.5% from NT$3.2 billion in 2010 to NT$3.5 billion in 2011. This increase was principally a result of an increase in research professionals and engineers.

Operating Costs and Expenses by Business Segment

	Domestic						
	Fixed Communications	**Mobile Communications**	**Internet**	**International Fixed Communications**	**Others**	**Adjustment**	**Total**
For the year ended December 31, 2011							
Operating costs and expenses	76.7	72.3	17.2	15.8	8.0	(27.6)	162.4
Depreciation and amortization	20.1	8.3	2.3	1.3	0.3		32.3
For the year ended December 31, 2010							
Operating costs and expenses	67.0	62.1	15.8	14.5	6.1	(20.5)	145.0
Depreciation and amortization	21.9	8.2	2.2	1.4	0.3		34.0

Domestic fixed communications

Our domestic fixed communications costs and expenses increased by 14.5% from NT$67.0 billion in 2010 to NT$76.7 billion in 2011, primarily due to an increase of NT$9.7 billion in interconnection and service expenses mainly due to the change in policy for collecting the tariffs of fixed-line-to-mobile phone calls. Since we are the market leader of the local call services, in addition to the interconnection fees, we are required to pay transition fees to the mobile operators for a period of six years.

Mobile communications

Our mobile communications operating costs and expenses increased by 16.4% from NT$62.1 billion in 2010 to NT$72.3 billion in 2011. This increase was primarily due to an increase of NT$7.9 billion in cost of handsets sold and an increase of NT$1.6 billion in leased line and internet access expenses.

Internet

Our internet operating costs and expenses increased by 9.1% from NT$15.8 billion in 2010 to NT$17.2 billion in 2011. This increase was primarily due to an increase of NT$0.8 billion in leased line expenses for broadband services and an increase of NT$0.4 billion in corporate solution services and ICT costs.

International fixed communications

Our international fixed communications costs and expenses increased by 9.2% from NT$14.5 billion in 2010 to NT$15.8 billion in 2011. The increase was primarily due to an increase of NT$0.9 billion in international interconnection expenses.

Others

The costs and expenses from our other business increased by 32.0 % from NT$6.1 billion in 2010 to NT$8.0 billion in 2011. The increase was primarily due to an increase of NT$1.4 billion in construction costs and an increase of NT$0.5 billion in research and development expense.

Income from operations and Operating Margin

As a result of the foregoing, our income from operations decreased by 4.0% from NT$57.4 billion in 2010 to NT$55.1 billion in 2011. Our operating margin decreased from 28.3% in 2010 to 25.3% in 2011.

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

	Domestic Fixed Communications	Mobile Communications	Internet	International Fixed Communications	Others	Adjustment	Total
				(in billions of NT$)			
For the year ended December 31, 2011							
Revenues from external customers	79.4	93.0	24.8	15.2	5.1		217.5
Intersegment service revenues	15.4	7.0	1.9	2.6	0.7	(27.6)	
Interest income					0.7		0.7
Other income	0.4	0.1		0.1	0.6		1.2
	95.2	100.1	26.7	17.9	7.1	(27.6)	219.4
Segment income before tax	18.5	27.8	9.6	2.0	(1.2)		56.7
For the year ended December 31, 2010							
Revenues from external customers	70.7	89.0	24.5	15.5	2.7		202.4

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	Domestic Fixed Communications	Mobile Communications	Internet	International Fixed Communications	Others	Adjustment	Total
				(in billions of NT$)			
Intersegment service revenues	14.7	2.1	1.1	1.7	0.7	(20.3)	
Interest income					0.5		0.5
Other income		0.3		0.1	0.3	(0.2)	0.5
	85.4	91.4	25.6	17.3	4.2	(20.5)	203.4
Segment income before tax	18.1	29.3	9.8	2.7	(2.2)		57.7

As a result of the foregoing, the segment income before tax for our domestic fixed communications business increased by 2.4% from NT$18.1 billion in 2010 to NT$18.5 billion in 2011; segment income before tax for our mobile communications business decreased by 5.1% from NT$29.3 billion in 2010 to NT$27.8 billion in 2011; segment income before tax for our internet business decreased by 2.8% from NT$9.8 billion in 2010 to NT$9.6 billion in 2011; segment income before tax for our international fixed communications business decreased by 23.1% from NT$2.7 billion in 2010 to NT$2.0 billion in 2011; and segment loss for our others business segment decreased by 43.7% from NT$2.2 billion in 2010 to NT$1.2 billion in 2011.

Other Income, Net

Our other income, net increased by 402.8% from NT$0.3 billion in 2010 to NT$1.6 billion in 2011. This increase was primarily due to a NT$0.5 billion increase in net gain on disposal of property, plant and equipment, a NT$0.2 billion increase in equity in earnings of equity method investees, a NT$0.3 billion increase in net interest income, and a NT$0.2 billion decrease in net loss on valuation and disposal of financial instruments.

Income Tax

Our income tax was NT$9.1 billion in 2010, compared to NT$8.6 billion in 2011. Our effective tax rate was 15.8% in 2010 and 15.2% in 2011, primarily due to lower income from operations. Please refer to Item 5. Operating and Financial Review and Prospects Taxation for a discussion of the change in tax rate.

Net Income

As a result of the foregoing, our net income attributable to stockholders of the parent decreased by 1.1% from NT$47.6 billion in 2010 to NT$47.1 billion in 2011. Our net margin was 23.5% in 2010 and 21.6 % in 2011.

B. Liquidity and Capital Resources

Liquidity

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

	For the year ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
		(in billions)		
Net cash provided by operating activities	84.8	75.3	67.5	2.3
Net cash used in investing activities	(17.4)	(33.1)	(38.9)	(1.3)
Net cash used in financing activities	(47.0)	(65.7)	(42.8)	(1.5)

Effect of exchange rate changes		0.1		
Effect of change on consolidated subsidiaries	(2.8)	(0.1)		
Net increase (decrease) in cash and cash equivalents	17.6	(23.5)	(14.2)	(0.5)
Cash and cash equivalents at end of year	90.9	67.4	53.2	1.8

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

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In 2012, we generated NT$67.5 billion (US$2.3 billion) net cash from operating activities as compared to NT$75.3 billion in 2011. The decrease was primarily due to a NT$7.1 billion (US$0.2 billion) decrease in consolidated net income and the exemption of deposits that we collect from specific mobile subscribers in advance for bundling subsidized mobile handsets with service plans.

In 2011, we generated NT$75.3 billion net cash from operating activities as compared to NT$84.8 billion in 2010. The decrease was primarily due to a NT$6.0 billion decrease in cash flow from accounts receivable because starting from 2011, we brought our billing period for monthly fees in line with that for connection charges, and due to a NT$2.3 billion decrease in income from operations owing to the increased operating cash outflow which outnumbered the revenue in 2011.

Historically, net cash from operating activities has been sufficient to cover our capital expenditures, including ongoing expansion and modernization of our networks.

In 2012, net cash used in investing activities was NT$38.9 billion (US$1.3 billion), increasing by 5.8 million from NT$33.1 billion in 2011. The change was primarily due to the increase in acquisition of property, plant and equipment.

In 2011, net cash used in investing activities was NT$33.1 billion, an increase from NT$17.4 billion in 2010. The change was primarily due to the decrease in cash flow from disposal of available-for-sale financial instruments.

In 2012, our net cash used in financing activities totaled NT$42.8 billion (US$1.5 billion), which mainly included NT$42.4 billion (US$1.5 billion) of payment of dividends during that period.

In 2011, our net cash used in financing activities totaled NT$65.7 billion, which mainly reflected NT$42.9 billion of payment of dividends during that period and NT$19.4 billion of cash distribution to our stockholders for a capital reduction plan.

Capital Resources

We have historically financed our capital expenditure requirements with our cash flows from operations. In future years, we expect to have capital expenditure requirements for the ongoing expansion and upgrade of our networks, including 3G/HSPA/HSPA+/Dual cell HSPA+, FTTx, Wi-Fi/femtocell and service platforms, and future construction of LTE to migrate mobile and data service customers to higher contribution platforms. We also expect to make dividend payments on an ongoing basis. See Item 8. Financial Information A. Consolidated Statements and Other Financial Information . Furthermore, we may require working capital from time to time to finance purchases of materials for our maintenance and other overhead expenses. We expect to primarily rely on cash generated from operations and, to a lesser extent, loans from commercial banks to meet our planned capital expenditures, make our planned dividend payments, repay debts and fulfill other commitments over the next twelve months.

As of December 31, 2012, our primary source of liquidity was NT$53.2 billion (US$1.8 billion) in cash and cash equivalents.

As of December 31, 2012, our subsidiary, Chief Telecom, had short-term unsecured loans in the amount of NT$40 million (US$1.4 million) with interest rates ranging from 1.25% to 1.27%. As of December 31, 2012, Chief Telecom had long-term unsecured loans in the amount of NT$8 million (US$0.3 million) at an interest rate at 2.01% and due in 2013.

As of December 31, 2012, our subsidiary, Light Era Development Co., Ltd. had long-term secured loans in the amount of NT$2.1 billion (US$70.6 million) with interest rates ranging from 1.13% to 2.10%, with NT$0.3 billion due in 2014, NT$1.4 billion due in 2015, and NT$0.4 billion due in 2017.

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As of December 31, 2012, our subsidiary Chunghwa Precision Test Technology Co., Ltd. had a short-term unsecured loan of NT$4 million (US$0.1 million) at an interest rate at 1.53%.

As of December 31, 2012, our subsidiary Chunghwa Sochamp Technology Inc. had short-term unsecured loans of NT$67 million (US$2.3 million) at interest rates ranging from 1.38% to 2.40%.

As part of the government s effort to upgrade the existing telecommunication infrastructure, we and other public utility companies were required by the ROC government to contribute a total of NT$1.0 billion to a Piping Fund, administered by the Taipei City Government. This fund is used to finance various telecommunications infrastructure projects. We accounted for the contribution as other monetary assets on our consolidated balance sheets.

Note 29 to our consolidated financial statements included elsewhere in this annual report provides a description of the assets are pledged as collateral for long-term bank loans and contract deposits.

Capital Expenditures

Substantially all of our capital expenditures in 2010, 2011 and 2012 were made for operations in the Republic of China. We have financed our capital expenditures using cash flow from operations and bank loans. The following table sets forth a summary of our capital expenditures for the periods indicated.

	For the year ended December 31,					
	2010		2011		2012	
	(NT$ in billions, except percentages)					
Capital Expenditures:						
Domestic fixed communications business	14.2	58%	16.6	62%	19.6	59%
Mobile communications business	5.3	21	4.3	16	7.2	22
Internet business	1.9	8	3.8	14	3.4	10
International fixed communications business	1.8	7	1.5	6	2.4	7
Others	1.4	6	0.7	2	0.7	2
Total capital expenditures	24.6	100%	26.9	100%	33.3	100%

The following table sets forth a summary of our planned capital expenditures for the year ending December 31, 2013.

	For the year ending December 31, 2013 (NT$ in billions, except percentages)	
Capital Expenditures:		
Domestic fixed communications business	20.2	54.3%
Mobile communications business	9.0	24.2
Internet business	5.2	14.0
International fixed communications business	2.0	5.4
Others	0.8	2.1
Total capital expenditures	37.2	100%

We expect our total capital expenditures to be approximately NT$37.2 billion in 2013. In future periods, we expect our total capital expenditures to rise due to the launch of new businesses, FTTx network expansion, access bandwidth enhancement, service platforms, cloud computing, including cloud data center construction, 3G/HSPA/HSPA+/Dual cell HSPA+ mobile network expansion and submarine cables. We expect to finance these capital expenditures with our cash flows from operations and bank loans.

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Inflation

We do not believe that inflation in Taiwan has had a material impact on our results of operations in 2010, 2011 or 2012.

Recent Accounting Pronouncements

Transition to IFRS in 2013

See Item 3. Key Information D. Risk Factors Risks Relating to Our Company and the Taiwan Telecommunications Industry . While we have adopted Taiwan IFRS for ROC reporting purposes, we plan to adopt IFRS for certain filings with the SEC, including our annual reports on Form 20-F for the year ending December 31, 2013 and thereafter. Following our adoption of IFRS for SEC filing purposes, we will no longer be required to reconcile our consolidated financial statements with U.S. GAAP.

The significant differences between Taiwan IFRS and ROC GAAP that are relevant to us were disclosed in our 2012 full year financial reports prepared in accordance with ROC GAAP, which is available on our website http://www.cht.com.tw. The information contained on our website does not form a part of this annual report.

Taiwan IFRS differs from IFRS in certain significant respects, including to the extent that any new or amended standards or interpretations applicable under IFRS may not be timely endorsed by the FSC. For example, as of the date of this annual report, the FSC has not endorsed any accounting pronouncements issued by the International Accounting Standards Board after January 1, 2011. Therefore, these pronouncements will not be applicable to Taiwan IFRS until endorsed by the FSC. Some of the major differences between IFRS and Taiwan IFRS that are relevant to us as of the date of this annual report are set forth below.

- The income taxes on undistributed earnings should be recognized at the year of earnings under IFRS, while it should be recognized at the year of distribution under Taiwan IFRS.

- According to the laws and regulations applicable to state-owned enterprises in Taiwan, we recorded revenue from fixed-line 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 our additional paid-in capital was from unearned revenues from fixed-line services as of that date. Under IFRS, following the revenue recognition guidance, the above service revenue should be treated as deferred income and recognized over the time when the service is continuously provided. Therefore, upon our first adoption of IFRS, we should retrospectively decrease additional paid-in capital while increase retained earnings on the transition date of January 1, 2012. There is no difference in the recognition of unearned revenues or deferred income between IFRS and Taiwan IFRS. However, according to the guidance released by the Taiwan Stock Exchange Corporation, or TWSE, in March 2012, which is a part of Taiwan IFRS, the additional paid-in capital under ROC GAAP that is not specifically promulgated under Taiwan IFRS should not be adjusted on the transition date of January 1, 2012. Therefore, we retain such additional paid-in capital under Taiwan IFRS.

It is difficult for us to evaluate the precise impact of the adoption of Taiwan IFRS and IFRS on our financial reporting generally, or on our financial statements for the year ending December 31, 2013 or the year ended December 31, 2012, because the FSC may issue new rules governing the adoption of Taiwan IFRS and as other laws and regulations may be amended with the adoption of Taiwan IFRS.

Upon our first adoption of Taiwan IFRS, we are required to apply Taiwan IFRS retrospectively unless otherwise exempted from certain applications and to present the opening balance sheet on the transition date of January 1, 2012 with adjusted opening balances prepared under Taiwan IFRS. Any transactions after the transition date are accounted for in accordance with Taiwan IFRS. Consequently, our consolidated financial statements for the year ended December 31, 2012 to be included in our annual report for the year ended December 31, 2013 may differ materially from those included in this annual report, even though they relate to the same fiscal year. Similarly, the selected comparison financial information to be included in our quarterly earnings releases in 2013 may differ materially from those released historically.

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Other recent accounting pronouncements

In May 2011, the Financial Accounting Standards Board (FASB) issued an accounting update to amend the fair value measurement guidance and include some enhanced disclosure requirements. The most significant change in disclosures is an expansion of the information required for Level 3 measurements based on unobservable inputs. The standard is effective for us for the year ended December 31, 2012. We have included these new disclosure, as applicable, in note 35 to our consolidated financial statements included elsewhere in this annual report.

In June and December 2011, the FASB issued accounting updates to eliminate the current option to report other comprehensive income and its components in the statement of stockholders equity. Instead, an entity will be required to present items of net income and other comprehensive income in one continuous statement or in two separate, but consecutive, statements. The new requirements do not change which components of comprehensive income are recognized in net income or other comprehensive income, or when an item of other comprehensive income must be reclassified to net income. The standard is effective for us for the year ended December 31, 2012. We have reported other comprehensive income and its components in two separate but consecutive statements and the adoption did not have an impact on its results of operations, financial position or cash flows.

In September 2011, the FASB issued an accounting update, which is intended to reduce the cost and complexity of the annual goodwill impairment test by providing entities an option to perform a qualitative assessment to determine whether further impairment testing is necessary. Specifically, an entity has the option to first assess qualitative factors to determine whether it is necessary to perform the current two-step test. If an entity believes, as a result of its qualitative assessment, that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is required. Otherwise, no further testing is required. This standard is effective for us for the year ended December 31, 2012. The adoption of this guidance did not have a material impact on our results of operations, financial position or cash flows.

In December 2011, the FASB issued an accounting update, which creates new disclosure requirements regarding the nature of an entity s rights of setoff and related arrangements associated with its financial instruments and derivative instruments. Certain disclosures of the amounts of certain instruments subject to enforceable master netting arrangements or similar agreements would be required, irrespective of whether the entity has elected to offset those instruments in the statement of financial position. The disclosure requirements are effective for annual reporting periods beginning on or after January 1, 2013 with retrospective application required. Since we adopted IFRS for our fiscal year 2013, we will no longer adopt this standard.

In February 2013, the FASB issued an accounting update requiring entities to present information about significant items reclassified out of accumulated other comprehensive income (loss) by component either on the face of the statement where net income is presented or as a separate disclosure in the notes to the financial statements. This standard is effective for the companies for the year ending December 31, 2013. Since we adopted IFRS for our fiscal year 2013, we will no longer adopt this standard.

U.S. GAAP Reconciliation

Our consolidated financial statements are prepared in accordance with ROC GAAP, which differ in certain material respects from U.S. GAAP. The following table sets forth a comparison of our net income and stockholders equity in accordance with ROC GAAP and U.S. GAAP as of and for the periods indicated.

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	For the year ended December 31,			
	2010	2011	2012	
	NT$	NT$	NT$	US$
	(in billions)			
ROC GAAP:				
Consolidated net income	48.6	48.1	41.0	1.4
Attributable to:				
Stockholders of the parent	47.6	47.1	39.9	1.4
Minority interests	1.0	1.0	1.1	
U.S. GAAP:				
Net income	49.2	49.4	42.6	1.5
Attributable to:				
Stockholders of the parent	48.3	48.4	41.5	1.4
Noncontrolling interests	0.9	1.0	1.1	0.1
Total stockholders equity:				
ROC GAAP	368.6	373.0	369.9	12.7
U.S. GAAP	296.1	301.4	299.7	10.3

Note 34 to our consolidated financial statements included elsewhere in this annual report provides a description of the significant differences between ROC GAAP and U.S. GAAP as they related to us and a reconciliation of net income and stockholders equity.

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

Research and Development

Our research and development efforts are focused on the development of advanced network services and operation technologies as well as the development of core technologies for the domestic telecommunications market. For 2010, 2011 and 2012, our research and development expenses were approximately NT$3.2 billion, NT$3.5 billion and NT$3.7 billion (US$0.1 billion), respectively, or approximately 1.6%, 1.6% and 1.7% of our revenues, respectively.

As of March 31, 2013, we had 2,474 researchers focusing on the following areas:

- wireless communication;
- broadband networks;
- network management;
- business management information;
- billing information;
- information and communication security;
- business and marketing strategy;

convergence services;

business solutions;

internet of things; and

cloud computing.

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We have developed a number of advanced network services, operation technologies and applications and value-added services, including our xDSL/FTTx deployment, internet-based call center, e-commerce platform, mobile internet services, global standard for mobile communications billing system, a new telecommunications operation service system for all business units of our company, government public key infrastructure, a leased line testing and monitoring system and an intelligent transportation system. As of December 31, 2012, we have been granted 473 domestic patents and 121 foreign patents.

D. Trend Information

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

E. Off-Balance Sheet Arrangements

Notes 29 and 30 to our consolidated financial statements included elsewhere in this annual report provide descriptions of the pledged assets, and significant commitments and contingencies. There are no off-balance sheet arrangements that are material to investors.

F. Tabular Disclosure of Contractual Obligations

Set forth below are our total contractual obligations as of December 31, 2012.

	Payments due by period				
	Total	Less than 1 Year	1-3 years	3-5 years	More than 5 years
	(NT$ in billions)				
Contractual Obligations(1)					
Short-term loans	0.1	0.1			
Long-term loans	2.1		1.7	0.4	
Obligations related to ST-2 satellite	2.6	0.2	0.4	0.4	1.6
Operating leases(2)	7.0	2.3	3.1	1.4	0.2
Total	11.8	2.6	5.2	2.2	1.8

(1) Accrued pension liabilities of NT$2.5 billion (US$87.4 million) as of December 31, 2012 have not been included in the table above.
(2) Operating leases obligations are described in note 30 to our consolidated financial statements included elsewhere in the annual report.

As of December 31, 2012, we had remaining commitments under non-cancelable contracts with various parties, including acquisition of lands and buildings of NT$30.9 million (US$1.1 million), acquisition of telecommunications equipment of NT$25.8 billion (US$889.5 million), unused letters of credit of NT$150.0 million (US$5.2 million) and contracts for printing bills, envelopes and marketing gifts of NT$17.8 million (US$0.6 million).

G. Foreign Exchange

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

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ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. Directors and Senior Management

The following table sets forth the name, age, position and tenure of each of our directors and supervisors and such person s position as of April 1, 2013. There is no family relationship among any of these persons. All of our directors and supervisors were elected at our annual general stockholders meeting held on June 18, 2010 and have terms from June 18, 2010 to June 17, 2013.

Name	Age	Position
Yen-Sung Lee	64	Chairman, chief executive officer and director
Mu-Piao Shih	60	President and director
Shyue-Ching Lu	64	Director
Jeng-Fang Jong	57	Director
Yu-Fen Hong	56	Director
Gordon S. Chen	59	Director
Yi-Bing Lin	52	Director
Shih-Wei Pan	58	Director
Chung-Yu Wang(1)	68	Director
Zse-Hong Tsai(1)	52	Director
Chung-Fern Wu(1)	56	Director
Shih-Peng Tsai	64	Director
I-Chuan Liou	65	Supervisor
I-Hwa Wu	64	Supervisor
Su-Ghen Huang	48	Supervisor

(1) Independent director.

Yen-Sung Lee is the chairman, chief executive officer and director of our company starting April 1, 2013. Dr. Lee was the president of our company from August 29, 2012 to April 1, 2013. From September 2008 until he was appointed as our president, Dr. Lee has served as a senior executive vice president of our company, supervising the marketing and IT department. Prior to that, Dr. Lee was the manager of our Enterprise Business Group from February 2007 to September 2008. Dr. Lee holds a Ph.D. degree in information engineering from National Chiao Tung University in Taiwan.

Mu-Piao Shih is the president of our company. Mr. Shih was a senior executive vice president of our company from August 2011 to April 1, 2013. Mr. Shih was an executive vice president of our company and the manager of our Mobile Business Group from September 2009 to August 2011. Mr. Shih served as an assistant vice president and a deputy manager of our Mobile Business Group from March 2005 to September 2009. He also served as the senior chief engineer of our Mobile Business Group from October 2001 to March 2005. Mr. Shih holds a master s degree in electronic engineering from the National Taiwan University.

Shyue-Ching Lu is a director of our company. Dr. Lu was the chief executive officer, a director and chairman of our company from August 2008 to April 1, 2013. Dr. Lu had served as our president from May 1996 until he was appointed our chairman in August 2008. Prior to that, Dr. Lu was the Director General of the Department of Posts and Communications of the Ministry of Transportation and Communications from 1993 to 1994 and the deputy director general of the Directorate General of Telecommunications from 1994 to 1996. Dr. Lu holds a Ph.D. degree in electrical engineering from the University of Hawaii and a bachelor s degree in engineering from the National Cheng Kung University in Taiwan.

Jeng-Fang Jong is a director of our company. Mr. Jong is also a director of Personnel Department at the Ministry of Transportation and Communications. Mr. Jong received his bachelor s degree from the National Taiwan college of Education.

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Yu-Fen Hong is a director of our company. Ms. Hong is currently the director of the accounting department at the Ministry of Transportation and Communications. She holds a master s degree in business & management from the National Chiao Tung University in Taiwan.

Gordon S. Chen is a director of our company, and also the Chairman of Gre Tai Securities Market. Dr. Chen has more than 28 years of services in financial sector. He gained in-depth financial expertise and hands-on banking experience from several government positions, such as chairman of TWSE Corporation and chairman of Taiwan Certificate Authority Corporation. Dr. Chen obtained a Ph.D. degree from the National Taiwan University, a master s degree in public finance from National Chengchi University and a bachelor s degree in economics at the Chinese Culture University.

Yi-Bing Lin is a director of our company. Dr. Yi-Bing Lin received his bachelor s degree from the National Cheng Kung University in Tainan, Taiwan in 1983, and his Ph.D. from the University of Washington in Seattle in 1990. From 1990 to 1995, he was a research scientist with Bellcore (Telcordia). He then joined the National Chiao Tung University, or NCTU, in Taiwan where he remains. In 1996, he served as the deputy director of Microelectronics and Information Systems Research Center at the NCTU. Between 1997 and 1999, Dr. Lin was chairman of the Department of Computer Science & Information Engineering at the NCTU. Since 2000, he has also been appointed as an adjunct research fellow at the Academia Sinica. Between 2004 and 2006, Dr. Lin was appointed the vice president of the office of research and development at the NCTU. From 2007 to February 22, 2011, Dr. Lin has served as the dean of the College of Computer Science at the NCTU. Since February 23, 2011, he became the vice president of NCTU.

Shih-Wei Pan is a director of our company. Dr. Pan is also currently the minister at the Council of Labor Affairs. Dr. Pan holds a Ph.D. degree in industrial and labor relations from Cornell University.

Chung-Yu Wang is currently an independent director of our company and also the former chairman of China Steel Corporation. He graduated from Chung Yuan Christian University with a bachelor s degree in chemical engineering.

Zse-Hong Tsai is an independent director of our company. Dr. Tsai is also currently a professor of electrical engineering at the National Taiwan University. His research interest includes broadband networking, performance evaluation and telecommunication regulations. Dr. Tsai holds a Ph.D. degree and a master s of science degree in electrical engineering from the University of California, Los Angeles, and a bachelor s of science degree in electrical engineering from the National Taiwan University.

Chung-Fern Wu is an independent director of our company. Dr. Wu is also currently a professor of Accounting at the National Taiwan University. She holds an MBA degree in finance and a bachelor s degree in accounting from the National Taiwan University. She started her career as a practicing CPA in Taiwan and a Systems Analyst in U.S.A. She started her academic career as an Assistant Professor in the Fisher School of Accounting, University of Florida after receiving her Ph.D. degree in accounting and information management from the Anderson Graduate School of Management, University of California, Los Angeles.

Shih-Peng Tsai is a director of our company. Mr. Tsai is currently a representative of the Member s Convention of the Chunghwa Telecom Workers Union. Mr. Tsai graduated from Ta Tung Junior Technological College of commerce.

I-chuan Liou is a supervisor of our company. Mr. Liou is the general director of Department of Education, Science and Culture of Executive Yuan. He holds a master s degree in education from National Taiwan Normal University.

I-Hwa Wu is a supervisor of our company. Ms. Wu is also the vice president of Chunghwa Post Co., Ltd. She holds a bachelor s degree in commerce of the National Taiwan University.

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Su-Ghen Huang is a supervisor of our company. Ms. Huang is also currently the director of the Department of Planning of the Directorate General of Budget, Accounting and Statistics at the Executive Yuan. Ms. Huang holds a bachelor s degree in accounting from the Furen University in Taiwan.

The following people served as directors and supervisors on our board during 2012 but are no longer serving with us due to resignations or replacements.

Shaio-Tung Chang was the president of our company. Mr. Chang served as a senior vice president of our company from March 2007 to August 2008 and an executive vice president of our company and manager of our Mobile Business Group from July 2004 to March 2007. He also served as executive vice president of our company and manager of our International Business Group from December 2002 to July 2004. Mr. Chang holds a master s degree in management science from the National Chiao Tung University in Taiwan.

Wen-Tsan Lin was a director of our company. Mr. Lin is also the General secretary of DGPA, or Directorate-General of Personnel Administration of Executive Yuan. Mr. Lin holds a Ph.D. degree in public administration from National Chengchi University in Taiwan.

Jennifer Yuh-Jen Wu was a director of our company. Dr. Wu is currently the Consultant of Ministry of Economic Affairs. Dr. Wu was the deputy director general of the Institute of Transportation at the Ministry of Transportation and Communications from 2008 to 2013. Dr. Wu holds a Ph.D. degree from the Institute of Traffic and Transportation from the National Chiao Tung University. She also holds two master s degrees from Northwestern University, one in electrical engineering and computer science and one in industrial engineering and management science.

Shwu-Fen Chao was a supervisor of our company. Ms. Chao is the Councilor to the Vice President of Republic of China. Ms. Chao was a Senior Specialist of the Department of Information and Tourism, Taipei City Government from 2006 to 2009 and the Secretary of the Taipei Economic and Cultural Representative Office in New Zealand from 1994 to 1996. She holds a master s degree in diplomacy from National Chengchi University.

The following table sets forth the name, age, position and tenure of each of our executive officers and such person s position as of April 1, 2013. There is no family relationship among any of these persons.

Name	Age	Position
Shu Yeh	55	Chief financial officer and senior executive vice president
Chi-Mau Sheih	59	Senior executive vice president
Cheng-Kann Wu	64	Senior executive vice president
Yuan-Kuang Tu	57	President of Business Group
Min-Hsuan Lin	64	President of Business Group
Kuo-Feng Lin	57	President of Business Group
Fu-Kuei Chung	59	President of Business Group
Hsiu-Gu Huang	60	President of Business Group
Tai-Feng Leng	64	President of Business Group
Feng-Yue Hung	63	President of Business Group
Shyang-Yih Chen	61	President of Business Group

Shu Yeh is our chief financial officer and senior executive vice president. Dr. Yeh is also a director of Chunghwa Investment Co., Ltd. Dr. Yeh served as an independent director of our company from June 2007 to January 2010. Dr. Yeh also served as a professor of accounting at National Taiwan University. Dr. Yeh holds a Ph.D. degree in accounting from the University of California, Los Angeles, a master s degree in professional accounting from the University of Texas at Austin, and a bachelor s degree in economics from the National Taiwan University.

Chi-Mau Sheih is a senior executive vice president of our company. Mr. Sheih is also a director of Senao International Co., Ltd. Mr. Sheih was an executive vice president and the manager of our Southern Taiwan Business Group from March 2007 to June 2010. Prior to that, he was an executive vice president of our company and the manager of our Central Taiwan Business Group from September 2006 to March 2007. He served as the senior managing director of our Network Department from September 2001 to January 2004. He also served as an assistant vice president of our company and a deputy manager of our Central Taiwan Business Group from January 2004 to September 2006. Mr. Sheih holds a master s degree in business administration from the National Taiwan University.

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Cheng-Kann Wu is a senior executive vice president of our company. Mr. Wu was the chief audit executive of our company from July 2011 to August 2012. Prior to that, he served as the deputy manager of our Northern Taiwan Business Group from March 2008 to July 2011. He also served as the managing director of our Accounting Department from July 2004 to March 2008. Mr. Wu holds a master s degree in management science from the National Chiao Tung University

Yuan-Kuang Tu is the president of our Northern Taiwan Business Group. Dr. Tu is also a director of Senao International Co., Ltd. He served as the president of Chunghwa Telecom Laboratories from May 2009 to March 2012, the senior managing director of our Corporate Planning Department from May 2007 to May 2009, and a vice president of Chunghwa Telecom Laboratories from March 2006 to April 2007. He holds a Ph.D. degree in electrical engineering from National Taiwan University.

Min-Hsuan Lin is the president of our Southern Taiwan Business Group since June 2010. Prior to that, he served as an assistant vice president of our company and a deputy manager of our Southern Taiwan Business Group from September 2009 to June 2010. He also served as the manager of the Tainan Branch Office from May 2007 to September 2009. He also served as the manager of the Fong-Shan Branch Office from February 2006 to May 2007, and he also served as the managing director of the Marketing Department of our Southern Taiwan Business Group from August 2004 to February 2006. Mr. Lin holds a bachelor s degree in transportation and communication management science from the National Cheng Kung University.

Kuo-Feng Lin is the president of our Mobile Business Group. Mr. Lin served as a deputy manager of our Mobil business group from October 2009 to May 2012. Prior to that, he served as the manager of Taipei Branch, Mobile Business Group from April 2006 to October 2009. Mr. Lin holds a bachelor s degree in electronic engineering from National Taipei Institute of Technology.

Fu-Kuei Chung is the president of our Data Communications Business Group. He is also a director of Chunghwa Telecom Vietnam Co., Ltd. Before promoting to this position, he previously served as a deputy manager of our Data Communications Business Group from September 2010 to 2012 March and the senior managing director of our Corporate Planning Departing from May 2009 to August 2010. Mr. Chung holds the master s degree in information management from National Taiwan University.

Hsiu-Gu Huang is the president of our Enterprise Business Group. Mr. Huang is also a director of China Airlines Co., Ltd. Mr. Huang served as an assistant vice president of our company and a deputy manager of our Enterprise Business Group from January 2007 to September 2008. Mr. Huang holds a master s degree in management science from the National Chiao Tung University in Taiwan.

Tai-Feng Leng is the president of the International Business Group. Miss Leng is also a director of Chief Telecom Inc., Donghwa Telecom Co., Ltd. and Chunghwa Telecom Singapore Pte., Ltd. Miss Leng served as the deputy manager of our International Business Group from July 2004 to December 2007 and as the senior managing director of our Marketing Department from October 2001 to July 2004. Miss Leng holds a master s degree in management science from the National Chiao Tung University in Taiwan.

Feng-Yue Hung is the president of our Telecommunication Laboratories. Mr. Hung served as the president of our Telecommunication Training Institute from December 2010 to March 2012. Prior to that, he served as the deputy manager of our Enterprise Business Group from September 2008 to December 2010 and served as the Director of our Information Technology Department from January 2006 to September 2008. Mr. Hung holds a master s degree in electronic from National Chiao Tung University.

Shyang-Yih Chen is the president of our Telecommunication Training Institute. Mr. Chen served as an executive vice president of our company and the manager of the Data Communication Business Group from September 2006 to March 2012. Prior to that, he served as the deputy manager of our Data Communication Business Group from January 2005 to September 2006. Mr. Chen holds a master s degree in electrical engineering from National Taiwan University.

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The following person served as our executive officer during 2012 but is no longer serving with us due to resignations or replacements.

Chang-Rong Chen was an executive vice president of our company and the manager of our Mobile Business Group. Mr. Chen was also a director of Chunghwa Investment Co., Ltd. Mr. Chen served as an assistant vice president and deputy manager of our Mobile Business Group from February 2006 to September 2011, and he also served as the managing director of the Marketing Department of our Mobile Business Group from March 2004 to February 2006. Mr. Chen holds a master s degree in business management from National Chiao Tung University.

B. Compensation

The compensation plan for our directors and supervisors was approved at our annual general stockholders meeting in 2006. The adjustment in the fixed monthly income for the president was approved by the compensation committee in October 2012. See C. Board Practices for a discussion of our compensation committee.

- the chairman of our board of directors may receive a fixed monthly income of NT$330,000 and a non-fixed income, including but not limited to performance-related bonuses or other rewards, which may not exceed his fixed income. The chairman will not receive any additional compensation for his role as a director;

- our president may receive a fixed monthly income of NT$305,000 and a non-fixed income, including but not limited to performance-related bonuses or other rewards, which may not exceed his fixed income. The president will not receive any additional compensation for his role as a director;

- independent directors who concurrently serve in military, public office or hold teaching or administrative post may receive a fixed monthly compensation of NT$8,000, and those who do not concurrently serve in military or public office or hold teaching or administrative post may receive a monthly compensation of NT$50,000; and

- directors and supervisors who serve in military, public office or hold teaching or administrative post may receive a monthly compensation of NT$8,000, and those directors and supervisors who do not serve in military and public office or hold teaching or administrative post may receive a monthly compensation of NT$30,000.

Any compensation above the stipulated amounts in the compensation plan for our directors and supervisors, including but not limited to profit-based bonuses, received by our directors and supervisors who are serving as representatives of the Ministry of Transportation and Communications or other legal persons will be collected by the Ministry of Transportation and Communications or the legal persons they represent, respectively. Our chairman, president, and labor representative to our board of directors Shyue-Ching Lu, Shaio-Tung Chang, Yen-Sung Lee, and Shih-Peng Tsai, respectively do not receive monthly compensation for acting as our directors because they receive salaries as employees.

The compensation plan was put into practice on January 1, 2006. The aggregate amount of compensation that we paid to our directors, supervisors and executive officers in 2010, 2011 and 2012 was NT$139,477,758, NT$136,289,017 and NT$140,141,488 (US$4,824,147.6), respectively. The aggregate amount of compensation in 2012 includes a NT$85,282,511 (US$2,935,714.7) salary payment for directors, supervisors and executive officers, a NT$8,638,918 (US$297,381.0) pension accrued for executive officers, a NT$37,483,664 (US$1,290,315.5) bonus for directors and supervisors and a NT$8,736,395 (US$300,736.5) bonus for executive officers and a labor union director. The 2012 bonus for our directors and supervisors may not exceed 0.2% of our distributable earnings and must be approved at our 2013 annual general stockholders meeting. See Item 5. Operating and Financial Review and Prospects Overview Provisions for pension payments to our employees and note 27 to our consolidated financial statements included elsewhere in this annual report for descriptions about our pension plans.

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Pursuant to ROC disclosure rules, we have disclosed the compensation of our directors and supervisors and the compensation range of our senior management for the fiscal year ended December 31, 2012 as follows:

Directors	Total Compensation	Fixed Income	Dividends	Business Expenses
		(in NT$)		
Chung-Yu Wang	626,000	600,000	(6)	26,000
Zse-Hong Tsai	632,000	600,000	(6)	32,000
Chung-Fern Wu	626,000	600,000	(6)	26,000
Shyue-Ching Lu	8,150,890 (1)		(7)	
Shaio-Tung Chang	6,345,471 (2)		(7)	
Yen-Sung Lee	6,307,589 (3)		(7)	
Shih-Peng Tsai	1,759,666 (4)	120,000	(7)	2,000
Wen-Tsan Lin	102,000	96,000	(7)	6,000
Yu-Fen Hong	100,000	96,000	(7)	4,000
Jennifer Yuh-Jen Wu	110,000	96,000	(7)	14,000
Shih-Wei Pan	98,000	96,000	(7)	2,000
Gordon S. Chen	366,000	360,000	(7)	6,000
Yi-Bing Lin	112,000	96,000	(7)	16,000
Ministry of Transportation and Communications(5)	28,112,750		28,112,750	

(1) NT$8,150,890 received as salary for serving as our chief executive officer.
(2) NT$6,345,471 received as salary for serving as our president.
(3) NT$5,635,667 received as salary for serving as our senior executive vice president and president, and NT$671,922 received as bonuses as our employee.
(4) Includes NT$1,543,193 received as salary and NT$94,473 received as bonuses as our employee and NT$122,000 received as compensation for serving as our director after retiring as our employee.
(5) Our juridical director.
(6) The independent directors will not receive any dividend distributions.
(7) Each of these directors is a legal representative of the MOTC. The dividend distributions will be paid directly to the MOTC because such dividend distributions are not the individual income of these directors.

Supervisors	Total Compensation	Fixed Income	Earnings Distributions	Business Expenses
		(in NT$)		
I-Chuan Liou(1)	50,710	46,710	(4)	4,000
Shwu-Fen Chao(2)	49,548	49,548	(4)	
I-Hwa Wu	106,000	96,000	(4)	10,000
Su-Ghen Huang	110,000	96,000	(4)	14,000
National Development Fund, Executive Yuan(3)	3,123,638		3,123,638(4)	