ALPHA NETWORKS INC. AND SUBSIDIARIES

Consolidated Financial Statements

December 31, 2007 and 2006
(With Independent Auditors’ Report Thereon)

Independent Auditors' Report

The Board of Directors
Alpha Networks Inc.:

We have audited the consolidated balance sheets of Alpha Networks Inc. and subsidiaries (the "Company") as of December 31, 2007 and 2006, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the consolidated financial statements of Des Voeux Ltd., which statements reflect total assets of NT$22,958 thousand and NT$38,834 thousand as of December 31, 2007 and 2006, respectively, and total revenue of NT$0 for the years ended December 31, 2007 and 2006. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Des Voeux Ltd., is based solely on the report of the other auditors.

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

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Alpha Networks Inc. and subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the Republic of China.

Hsinchu, Taiwan (Republic of China)
February 29, 2008

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

ALPHA NETWORKS INC. AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2007 and 2006
(in thousands of New Taiwan dollars)

Assets	2007	2006
Current assets:		
Cash and cash equivalents (note 4)	$ 3,135,406	3,097,024
Financial assets at fair value through profit or loss—current (note 6)	510	944
Notes and accounts receivable, net (note 7)	2,585,216	2,367,749
Receivables from related parties (note 16)	3,085,289	2,719,558
Other financial assets—current (note 15)	32,356	15,403
Inventories (note 8)	2,144,622	2,063,223
Other current assets (note 13)	60,620	106,537
	11,044,019	10,370,438
Funds and investments:		
Other financial assets—noncurrent (note 15)	36,187	32,711
Available-for-sale financial assets—noncurrent (note 5)	57,300	-
Financial assets carried at cost—noncurrent (note 5)	9,996	3,274
	103,483	35,985
Property, plant and equipment (notes 6 and 14):		
Buildings and improvements	1,675,234	1,590,789
Machinery and equipment	1,384,015	1,206,036
Transportation, office and other equipment	257,692	236,860
	3,316,941	3,033,685
Less: accumulated depreciation	1,176,935	952,873
Prepayment for equipment and construction in progress	86,802	56,994
	2,226,808	2,137,806
Goodwill	140,913	134,883
Other assets:		
Deferred expenses and others	169,183	137,565
Deferred income tax assets—noncurrent (note 13)	743	481
	169,926	138,046
Total assets	$ 13,685,149	12,817,158

Liabilities and Stockholders' Equity	2007	2006
Current liabilities:		
Short-term borrowings (note 9)	$ 102,564	660,849
Accounts payable	3,603,346	3,249,533
Payables to related parties (note 16)	83,307	81,943
Accrued expenses	858,901	573,153
Payroll and bonus payable	415,078	279,670
Financial liabilities at fair value through profit or loss—current (note 6)	13,460	8,777
Bonds payable—current portion (note 10)	389,481	-
Other current liabilities	236,682	402,118
	5,702,819	5,256,043
Long-term liabilities:		
Financial liabilities at fair value through profit or loss—noncurrent	-	17,508
Bonds payable (note 10)	-	1,076,934
	-	1,094,442
Other liabilities:		
Accrued pension liabilities (note 11)	73,132	71,181
Deferred credit	160	215
	73,292	71,396
Total liabilities	5,776,111	6,421,881
Stockholders' equity (note 12)**:**		
Common stock	4,062,872	3,554,372
Advance receipts for common stock	53,164	-
	4,116,036	3,554,372
Capital surplus	1,522,981	1,070,418
Retained earnings:		
Legal reserve	282,168	177,328
Unappropriated earnings	1,870,227	1,536,633
	2,152,395	1,713,961
Cumulative foreign currency translation adjustment	111,307	56,526
Unrealized gain or loss on available-for-sale financial assets	323	-
Minority interest	5,996	-
Total stockholders' equity	7,909,038	6,395,277
Total liabilities and stockholders' equity	$ 13,685,149	12,817,158

See accompanying notes to consolidated financial statements.

ALPHA NETWORKS INC. AND SUBSIDIARIES

Consolidated Statements of Income

Years ended December 31, 2007 and 2006
(in thousands of New Taiwan dollars, except for net income per common share)

		2007	2006
Sales (note 16)	$	22803,697	21,556,029
Less: sales returns and allowances		452,267	86,875
		22,351,430	21,469,154
Cost of goods sold (note 16)		18,301,438	18,006,885
Gross profit		4,049,992	3,462,269
Operating expenses (note 16)**:**			
Selling		643,067	545,330
General and administrative		393,583	379,571
Research and development		1,328,938	1,058,020
		2,365,588	1,982,921
Operating income		1,684,404	1,479,348
Non-operating income and gains:			
Interest income		70,443	43,978
Foreign currency exchange gain, net		35,406	-
Gain on valuation of financial liabilities		4,048	16,259
Other income, net		-	30,066
		109,897	90,303
Non-operating expense and loss:			
Interest expense		49,938	71,473
Loss on valuation of financial assets		74,878	13,711
Foreign currency exchange loss, net		-	59,466
Loss on inventory obsolescence and devaluation		61,841	117,395
Other loss, net		50,922	-
		237,579	262,045
Income before income taxes		1,556,722	1,307,606
Income tax expenses (note 13)		262,978	272,724
Net income before cumulative effect of changes in accounting principle		1,293,744	1,034,396
Cumulative effect of changes in accounting principle (note 3)		-	13,514
Consolidated net income	**$**	**1,293,744**	**1,048,396**
Attributable to:			
Shareholders of the parent	$	1,293,758	1,034,396
Minority interests		(14)	-
	$	**1,293,744**	**1,048,396**

		2007 Before taxes	2007 After taxes	2006 Before taxes	2006 After taxes
Net income per common share (note 14)					
Basic earnings per common share:					
Net income before cumulative effect of changes in accounting principle	$	3.87	3.26	3.87	3.06
Cumulative effect of changes in accounting principle		-	-	0.05	0.04
	$	**3.87**	**3.26**	**3.92**	**3.10**
Diluted earnings per common share:					
Net income before cumulative effect of changes in accounting principle	$	3.59	3.02	3.49	2.76
Cumulative effect of changes in accounting principle		-	-	0.04	0.03
	$	**3.59**	**3.02**	**3.53**	**2.79**
Basic earnings per common share – retroactively adjusted				**$ 3.71**	**2.93**
Diluted earnings per common share – retroactively adjusted				**$ 3.34**	**2.63**

See accompanying notes to consolidated financial statements.

ALPHA NETWORKS INC. AND SUBSIDIARIES

Consolidated Statements of Changes in Stockholders' Equity

Years ended December 31, 2007 and 2006
(in thousands of New Taiwan dollars)

				Retained Earnings						
	Common stock	Advance receipts for common stock	Capital surplus	Legal reserve	Special reserve	Unappro-priated earnings	Cumulative foreign currency translation adjustment	Unrealized gain or loss on available-for-sale financial assets	Minority interest	Total stockholders' equity
Balance at January 1, 2006	$ 2,829,000	-	579,773	75,080	3,272	1,271,952	34,906	-	-	4,793,983
Appropriation of earnings:										
Legal reserve	-	-	-	102,248	-	(102,248)	-	-	-	-
Stock dividends	116,064	-	-	-	-	(116,064)	-	-	-	-
Bonuses to employees—stock	115,000	-	-	-	-	(115,000)	-	-	-	-
Cash dividends	-	-	-	-	-	(435,241)	-	-	-	(435,241)
Employees' bonuses	-	-	-	-	-	(29)	-	-	-	(29)
Directors' and supervisors' remuneration	-	-	-	-	-	(18,405)	-	-	-	(18,405)
Reversal of special reserve	-	-	-	-	(3,272)	3,272	-	-	-	-
Conversion options embedded in convertible bonds	-	-	113,640	-	-	-	-	-	-	113,640
Foreign currency translation adjustments	-	-	-	-	-	-	21,620	-	-	21,620
Capital surplus transferred to common stock	174,097	-	(174,097)	-	-					-
Issuance of stock for merger	217,801	-	528,192	-	-	-	-		-	745,993
Issuance of stock from exercising stock options	102,410	-	22,910	-	-	-	-	-	-	125,320
Net income for 2006	-	-	-	-	-	1,048,396	-	-	-	1,048,396
Balance at December 31, 2006	3,554,372	-	1,070,418	177,328	-	1,536,633	56,526	-	-	6,395,277
Appropriation of earnings:										
Legal reserve	-	-	-	104,840	-	(104,840)	-	-	-	-
Stock dividends	107,776	-	-	-	-	(107,776)	-	-	-	-
Bonuses to employees—stock	117,000	-	-	-	-	(117,000)	-	-	-	-
Cash dividends	-	-	-	-	-	(610,732)	-	-	-	(610,732)
Employees' bonuses	-	-	-	-	-	(945)	-	-	-	(945)
Directors' and supervisors' remuneration	-	-	-	-	-	(18,871)	-	-	-	(18,871)
Issuance of stock for conversion of bonds	231,054	25,474	452,563	-	-	-	-	-	-	709,091
Foreign currency translation adjustments	-	-	-	-	-	-	54,781	-	-	54,781
Issuance of stock for employee stock option exercised	52,670	27,690	-	-	-	-	-	-	-	80,360
Unrealized gains or losses on available-for-sale financial assets	-	-	-	-	-	-	-	323	-	323
Increased in minority interest	-	-	-	-	-	-	-	-	6,010	6,010
Net income for 2007	-	-	-	-	-	1,293,758	-	-	(14)	1,293,744
Balance at December 31, 2007	$ 4,062,872	53,164	1,522,981	282,168	-	1,870,227	111,307	323	5,996	7,909,038

See accompanying notes to consolidated financial statements.

ALPHA NETWORKS INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
Years ended December 31, 2007 and 2006
(in thousands of New Taiwan dollars)

		2007	2006
Cash flows from operating activities:			
Net income attributed to parent company's shareholders	$	1,293,758	1,048,396
Net income attributed to minority interest		(14)	-
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization		438,892	408,463
Provision (reversal) for allowance for doubtful accounts		21,399	(2,754)
Provision for inventory obsolescence and devaluation loss		80,770	117,395
Loss on impairment of long-term equity investments under cost method		3,274	13,711
Effect of valuation of financial assets and liabilities at fair value through profit or loss		(4,558)	(16,259)
Loss (gain) on disposal of property, plant and equipment		4,470	(23,328)
Amortization of discount on bonds payable		21,638	28,853
Unrealized exchange loss (gain)		(36,637)	39,753
Increase in inventories		(162,169)	(139,574)
Decrease in financial assets at fair value through profit or loss		944	26,716
Decrease (increase) in deferred income tax assets		(2,843)	10,734
Increase in notes and accounts receivable (including related parties)		(565,448)	(1,174,381)
Increase in accounts payable (including related parties)		351,029	661,750
Increase in accrued pension		1,951	2,021
Increase (decrease) in financial liabilities at fair value through profit or loss		(8,777)	5,343
Decrease (increase) in other operation-related current assets		13,286	(18,667)
Increase (decrease) in other operation-related current liabilities		275,582	(2,413)
Cash provided by operating activities		1,726,547	985,759
Cash flows from investing activities:			
Net cash paid for acquisition of subsidiary		(6,030)	-
Proceeds from disposal of property and equipment		934	22,497
Acquisition of property and equipment		(406,611)	(532,388)
Acquisition of financial assets carried at cost－noncurrent		(9,996)	-
Increase in available-for-sale financial assets－ noncurrent		(56,977)	-
Decrease (increase) in deposits and other assets		(11,808)	56,742
Increase in deferred expenses		(95,545)	(62,378)
Cash flows from merger		-	275,226
Return of capital from liquidation of long-term equity investments		134	-
Cash used in investing activities		(585,899)	(240,301)
Cash flows from financing activities:			
Increase (decrease) in short-term borrowings		(558,285)	641,903
Proceeds from issuance of stock for employee stock options exercised		80,360	125,320
Payments of cash dividends, directors' and supervisors' remuneration, and employees' bonuses		(630,548)	(453,675)
Issuance of bonds payable		-	1,200,000
Increase in minority interest		6,010	-
Cash provided by (used in) financing activities		(1,102,463)	1,513,548
Effect of exchange rate changes on cash		197	17,992
Net increase in cash and cash equivalents		38,382	2,276,998
Cash and cash equivalents at beginning of year		3,097,024	820,026
Cash and cash equivalents at end of year	$	3,135,406	3,097,024
Supplemental disclosures of cash flow information:			
Cash payments of interest	$	28,300	38,203
Cash payments of income taxes	$	170,751	253,019
Supplementary disclosure of non-cash investing and financial activities:			
Convertible bonds converted into common stock and capital surplus	$	709,091	-
Cash flows from merger:			
Issuance of common stock and capital surplus	$	-	745,993
Liabilities		-	145,308
Goodwill		-	(134,883)
Acquisition of non-cash assets		-	(481,192)
Cash provided from merger	$	-	275,226

See accompanying notes to consolidated financial statements.

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2007 and 2006
(amounts expressed in thousands of New Taiwan dollars, except for per share information and unless otherwise noted)

1. Organization and Principal Activities

Alpha Networks Inc. ("Alpha") was established by a spin-off whereby on August 16, 2003, D-Link Corporation ("D-Link") separated its original design manufacturing and original equipment manufacturing ("ODM/OEM") operations from its D-Link brand business and transferred related operating assets and liabilities to Alpha. Alpha was incorporated on September 4, 2003, as a company limited by shares under the laws of the Republic of China ("ROC") and the ROC Statute for the Establishment and Administration of the Science-Based Industrial Park. The shares of Alpha have been traded on the Taiwan Stock Exchange since December 20, 2004. Alpha set up a branch in Hsinchu on June 14, 2005. Based on the resolution of Alpha's board of directors on April 17, 2006, Alpha merged with Cellvision System Inc. (Cellvision) on October 1, 2006. Cellvision was eliminated in the procedure.

Alpha's main activities include the research, development, production and sale of broadband products, computer network systems, wireless local area networks ("LANs"), and relevant spare parts.

Cellvision's main activities include the research, development, production and sale of network print servers, file servers, internet cameras and servers, etc.

As of December 31, 2007, Alpha and subsidiaries had 6,340 employees.

2. Summary of Significant Accounting Policies

(1) The accompanying consolidated financial statements are prepared in accordance with accounting principles generally accepted in the Republic of China (ROC). The major accounting policies and measurement basis adopted in preparing the accompanying consolidated financial statements are summarized as follows:

(a) The consolidated subsidiaries of Alpha are summarized below.

Investor	Investee	Percentage of ownership at December 31, 2007	Percentage of ownership at December 31, 2006
Alpha	Alpha Solutions Co., Ltd. (Alpha Solutions)	100	100
Alpha	Redsonic Technology Co. (Redsonic)	-	100
Alpha	Alpha Holdings Inc. (Alpha Holdings)	100	100
Alpha	Des Voeux Ltd. (Des Voeux)	100	100

(Continued)

Investor	Investee	Percentage of ownership at December 31, 2007	Percentage of ownership at December 31, 2006
Alpha	Darson Trading Limited (Darson)	100	100
Alpha	Alpha Global Capital Corporation Limited (Alpha Global)	100	100
Alpha	Net Mag Technology Corp. (Net Mag)	100	-
Alpha	Aescu Technology Inc. (Aescu)	79.97	-
Alpha Holdings	D-Link Asia Investment Pte. Ltd. (D-Link Asia)	100	100
Alpha Holdings	Tong Ying Trading (Shenzhen) Co., Ltd. (Tong Ying)	100	100
Alpha Holdings	Alpha Networks (Chengdu) Co., Ltd. (Alpha Chengdu)	100	100
Alpha Holdings	Alpha Investment Pte. Ltd. (Alpha Investment)	100	100
Alpha Investment	Alpha Networks (Dongguan) Co., Ltd. (Alpha Dongguan)	100	100
D-Link Asia	Dongguan Youxun Electronics Co., Ltd. (Dongguan Youxun)	100	100
Des Voeux	Alpha Networks Inc. (Alpha U.S.A.)	100	100

(b) The details of changes in subsidiaries included in the consolidated financial statements:

Alpha incorporated Alpha Dongguan, Darson, and Alpha Global in 2006, and incorporated Net Mag and acquired Aescu in 2007. The subsidaries are included in the consolidated financial statements of the Company starting from 2006 and 2007.

Redsonci registered for liquidation with the governmental authorities in December 2007, and has been excluded from consolidation since that date.

(2) Basis of consolidation

The consolidated financial statements include the accounts of Alpha and its subsidiaries, referred to individually or collectively as "the Company", in which Alpha directly or indirectly owns over 50% of the voting shares and is able to exercise control over the subsidiaries' operations and financial policies. All significant inter-company transactions and balances are eliminated in consolidation.

(Continued)

(3) Use of estimates

The preparation of the consolidated financial statements requires management to make reasonable estimates and assumptions that affect the reported amount of assets, liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amount of revenues and expenses during the reporting periods. Actual results may differ from management's estimates.

(4) Foreign currency transactions and translation

Entities included in the consolidated financial statements record transactions in their respective functional currencies. Non-derivative foreign currency transactions are recorded at the exchange rates prevailing on the transaction date. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated using the exchange rates on that date. The resulting exchange gains or losses from settlement of such transactions or translation of foreign-currency-denominated monetary assets or liabilities are reflected as non-operating gains or losses in the accompanying consolidated statements of income.

Effective January 1, 2006, the Company adopted the newly revised Statement of Financial Accounting Standards No. 14 (SFAS No. 14) "The Effects of Changes in Foreign Exchange Rates". In accordance with the newly revised SFAS No. 14, non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated into New Taiwan dollars at rates prevailing at the balance sheet date. If the non-monetary assets or liabilities are measured at fair value through profit or loss, the resulting unrealized exchange gains or losses from such transactions are recorded in current profit or loss. If the non-monetary assets or liabilities are measured at fair value through stockholders' equity, then the resulting unrealized exchange gains or losses from such transactions are recorded as a separate component of stockholders' equity. Translation differences resulting from the Company's payments for foreign operating departments that are of a long-term investment or long-term advance nature are recorded in cumulative translation adjustment, a separate component of stockholders' equity.

In translating foreign currency financial statements into New Taiwan dollars, balance sheet date rates are used for asset and liability accounts; historical rates are used for equity accounts, except that the prior-year translated balance is carried forward for the beginning retained earnings; and weighted-average rates are used for profit and loss accounts. Translation differences are included in the cumulative translation adjustment account under stockholders' equity.

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(5) Principles of classifying assets and liabilities as current and non-current

Cash or cash equivalents that are not restricted in use, assets held for the purpose of trading, and assets that will be held for a short time period and are expected to be converted to cash within 12 months from the balance sheet date are recorded as current assets; otherwise, they are recorded as non-current assets.

Liabilities that are expected to be liquidated within 12 months after the balance sheet date are recorded as current liabilities; otherwise, they are recorded as non-current liabilities.

(6) Cash equivalents

The Company considers all highly liquid investments, such as investments in bonds with repurchase agreements, with a maturity of three months or less to be cash equivalents.

(7) Asset impairment

The Company adopted SFAS No. 35 “Impairment of Assets”. In accordance with SFAS 35, the Company assesses at each balance sheet date whether there is any indication that an asset (individual asset or cash-generating unit) other than goodwill may have been impaired. If any such indication exists, the Company estimates the recoverable amount of the asset. The Company recognizes impairment loss for an asset whose carrying value is higher than the recoverable amount. The Company reverses an impairment loss recognized in prior periods for assets other than goodwill if there is any indication that the impairment loss recognized no longer exists or has decreased. The carrying value after the reversal should not exceed the recoverable amount or the depreciated or amortized balance of the assets assuming no impairment loss was recognized in prior periods.

The Company assesses the cash-generating unit to which goodwill is allocated on an annual basis and recognizes an impairment loss on the excess of carrying value over the recoverable amount.

(8) Financial instruments

Effective January 1, 2006, the Company and subsidiaries adopted SFAS No. 34 “Financial Instruments: Recognition and Measurement”. In accordance with SFAS 34, financial instruments are classified as financial assets and liabilities measured at fair value through profit or loss, available-for-sale financial assets, and financial assets carried at cost.

The Company and subsidiaries adopted transaction (or settlement) date accounting for financial instrument transactions. Upon initial recognition, financial instruments are evaluated at fair value. Except for financial instruments held for trading purposes, acquisition cost or issuance cost is added to the originally recognized amount[K1].

(Continued)

After initial recognition, the Company and subsidiaries classify the financial instruments according to their purpose of holding or issuance as follows:

1. Financial assets (liabilities) at fair value through profit or loss

   Financial assets (liabilities) at fair value through profit or loss are held with the intention of buying and selling them in a short period of time. Except for those that the Company and subsidiaries hold for hedging purposes and are considered to be effective hedging instruments, financial derivatives are classified as into this account.

2. Available-for-sale financial assets

   The available-for-sale financial assets are measured at fair value, and the changes in fair value are reported as a separate component of stockholders' equity. If there is objective evidence that a financial asset is impaired, a loss is recognized. If, in a subsequent period, events or changes in circumstances indicated that the amount of impairment loss decreases, the previously recognized impairment loss for equity securities is reversed to the extent of the decrease and recorded as an adjustment to stockholders' equity. While for debt securities, the reversal is allowed through profit or loss provided that the decrease is clearly related to an event which occurs after the impairment loss is recognized.

3. Financial assets carried at cost

   Equity investments which could not be measured at fair value with reasonable certainty are carried at their initial cost. However, if there is objective evidence of impairment, a loss is recognized. Restoration of a previously recognized impairment loss is prohibited.

(9) Derivative financial instruments

The Company and subsidiaries uses derivative financial instruments to manage its exposure to foreign exchange and interest rate risks resulting from operational, financing, and investment activities. A financial instrument which is not effective for hedging purposes is classified as financial instrument measured at fair value through profit or loss.

(10) Allowance for doubtful accounts

The allowance for doubtful accounts is determined based on the ageing, credit evaluation results, past experience, and the Company's internal credit policies.

(11) Inventories

Inventories are stated at the lower of cost or market value. Cost is determined by the weighted-average method. The market value of raw materials is determined on the basis of replacement cost, and the market values of finished goods and work in process are determined on the basis of net realizable value.

(12) Property, plant and equipment

Property, plant and equipment are stated at cost. Costs associated with significant additions, improvements, and replacements to property, plant and equipment are capitalized. Repairs and maintenance are charged to expenses as incurred.

Depreciation of property, plant and equipment of the Company is provided for by using the straight-line method over the estimated useful lives of the respective assets. The useful lives of property, plant and equipment are as follows:

(a) Buildings and improvements: 5~50 years.
(b) Machinery and equipment: 3~8 years.
(c) Transportation: 3~5 years.
(d) Office equipment and others: 3~8 years.

Gains or losses on the disposal of property, plant and equipment are accounted for as non-operating income or losses in the consolidated statement of income.

(13) Intangible assets

Effective from January 1, 2007, the Company and subsidiaries adopted SFAS No. 37 "Intangible Assets". In accordance with SFAS No. 37, except when it forms part of the cost of a business combination, expenditure on research is recognized as an expense when it is incurred. An intangible asset arising from development shall be recognized if, and only if, a company can demonstrate all of the following:

(a) the technical feasibility of completing the intangible asset so that it will be available for use or sale.

(b) its intention to complete the intangible asset and use or sell it.

(c) its ability to use or sell the intangible asset.

(d) how the intangible asset will generate probable future economic benefits.

(e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.

(f) its ability to measure reliably the expenditure attributable to the intangible asset during its development.

Goodwill represents the excess of the cost of the acquisition over the Company's interest in the fair value of the identifiable assets, liabilities, and contingent liabilities of the acquired. Goodwill is measured at cost less accumulated impairment losses.

(Continued)

(14) Deferred expenses

The purchase costs of software and intellectual property rights are recorded as deferred expenses and are amortized over periods ranging from three to five years, on a straight-line basis.

(15) Convertible bonds

Effective January 1, 2006, convertible bonds issued by the Company involving financial liabilities and conversion options where the bondholder could elect to covert the bond into the Company's equity instrument are treated as compound financial instruments based on the SFAS No. 36. The issuance costs are allocated pro-rata to liability and equity elements of the convertible bonds based on their original recognition amount. The fair value of liability elements in convertible bonds is determined by reference to the fair value of similar liability which has no relation with the equity element. The amount of equity element is calculated by reducing the fair value of liability elements from the total value of convertible bonds. The interest expense of convertible bonds is calculated by the effective interest rate method and recorded in the consolidated statements of income over the duration of the bonds.

(16) Retirement plan

Alpha and Redsonic established employee non-contributory defined benefit retirement plans (the "Plans") covering all regular employees. In accordance with the Plans, the Company's employees are eligible for retirement or are required to retire after meeting certain age or service requirements. Payments of retirement benefits are based on years of service and the average salary for the six-month period before the employee's retirement. Each employee earns two months of salary for the first fifteen years of service, and one month of salary for each year of service thereafter. The maximum retirement benefit is 45 months of salary. Beginning July 1, 2005, pursuant to the ROC Labor Pension Act (hereinafter referred to as the "New Act"), employees who elected to participate in the new system or joined the Company after July 1, 2005, is covered by a defined contribution plan under the New Act. For these employees, the Company is required to make a monthly contribution at a rate no less than 6% of the employee's monthly wages to the employee's individual pension fund account at the ROC Bureau of Labor Insurance.

The defined benefit plan under the ROC Labor Standards Law (the "old system") is accounted for in according with ROC SFAS No. 18, "Accounting for Pensions" which requires an actuarial calculation of pension obligation at year-end. Based on the actuarial calculation, Alpha recognizes a minimum pension liability and net periodic pension costs covering the service lives of the retirement plan participants, including current service cost, net obligation at transition, and pension gains or losses amortized on a straight-line basis. In accordance with the requirement of the ROC Labor Standards Law, Alpha and Redsonic have contributed monthly at the rate of 2% of salaries and wages to a pension fund.

(Continued)

Under the New Act, Alpha, Redsonic, Net Mag, and Aescu contribute 6% of employees' monthly wages to the Bureau of Labor Insurance. The contribution for a period is recognized as pension cost for that period.

Alpha Holdings, Alpha Investments, Des Voeux, Alpha Global, Net Mag, Aescu, etc., did not establish pension plans, and therefore, no pension expense was recognized.

Darson, D-Link Asia, Tong Ying, Dongguan Youxun, Alpha Chengdu, Alpha Dogguan, Alpha U.S.A. and Alpha Solutions have defined contribution retirement plans, and the contribution for a period is recognized as pension cost for that period.

(17) Revenue recognition and allowance for sales returns and discounts

Sales revenue is recognized when title to the products and the risks and rewards of ownership are transferred to the customers, which occurs principally at the time of shipment. Outsourcing revenue is recognized when the conversion work has been completed and processed products are delivered. Allowance and related provisions for sales returns and discounts are estimated based on historical experience. Such provisions are deducted from sales in the year the products are sold.

(18) Income taxes

Income taxes are accounted for under the asset and liability method. Deferred income taxes are determined based on differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect during the years in which the differences are expected to reverse. The income tax effects resulting from taxable temporary differences are recognized as deferred income tax liabilities. The income tax effects resulting from deductible temporary differences and tax credits are recognized as deferred income tax assets. The realization of deferred income tax assets is evaluated, and if it is considered more likely than not that the deferred tax assets will not be realized, a valuation allowance is recognized accordingly.

Classification of deferred income tax assets or liabilities as current or non-current is based on the classification of the related asset or liability. If the deferred income tax asset or liability is not directly related to a specific asset or liability, then the classification is based on the expected realization date of such asset or liability.

The Company's purchase of machinery and technology for the automation of production and expenditures for research and development and for training entitle the Company to tax credits that are recognized by using the flow-through method.

According to the ROC Income Tax Act, undistributed earnings of Alpha and its subsidiaries in the ROC are subject to an additional 10 percent corporate income surtax. The surtax is charged to income tax expense after the appropriation of earnings is approved by the stockholders in the following year.

(Continued)

The income tax return of each consolidated entity is filed separately and could not be consolidated with Alpha's filing. The Company's income tax expense in the consolidated financial statements includes the accounts of Alpha and its subsidiaries.

(19) Earnings per common share

Earnings per common share are computed based on the weighted-average number of common shares outstanding during the period. The effect on earnings per common share from the increase in stock from the issuance of stock dividends from unappropriated earnings, capital surplus, and employee bonuses is computed retroactively.

Alpha's employee stock options and convertible bonds issued are regarded as potential common stock. If there is no dilutive effect, only basic net income per common share will be disclosed.

(20) Employee stock option plan

Alpha adopts the intrinsic value method to measure the compensation cost, which is the excess of the quoted market price of Alpha stock over the exercise price of employee stock options on the measurement date. Compensation cost is charged to expense over the employee service period, with a corresponding increase in stockholders' equity.

3. Reasons for and Effect of Changes in Accounting Principle

The Company and subsidiaries adopted SFAS No. 34 "Financial Instruments: Recognition and Measurement" and No. 36 "Financial Instruments: Presentation and Disclosure" on January 1, 2006. After reclassifying and measuring, the cumulative effect of changes in accounting principle amounted to $13,514 thousand. The adoption of the newly released SFASs resulted in an increase in net income and basic earnings per share of $16,259 thousand and $0.05, respectively, in 2006. The financial instruments' related information is disclosed in notes 6 and 15.

Effective January 1, 2006, the Company and subsidiaries adopted the newly revised SFAS No. 14 "The Effects of Changes in Foreign Exchange Rates". There was no effect on net income or basic earnings per share for the year ended December 31, 2006.

Effective January 1, 2007, the Company and subsidiaries adopted the newly announced SFAS No. 37 "Intangible Assets." The adoption of this new standard did not affect the income and basic earnings per share for the year ended December 31, 2007.

(Continued)

4. Cash and Cash Equivalents

		December31, 2007	December31, 2006
Cash on hand	$	4,829	49,160
Checking and savings accounts		493,463	208,084
Time deposits		2,537,114	1,473,570
Cash equivalents – bonds with repurchase agreements		100,000	1,366,210
	$	**3,135,406**	**3,097,024**

5. Financial Assets

		December31, 2007	December31, 2006
Available-for-sale financial assets – non-current:			
Publicly traded stock – D-Link Corp.	**$**	**57,300**	**-**
Financial assets carried at cost – non-current:			
TGC, Inc.	$	-	3,274
QuieTek Corp.		9,996	-
	$	**9,996**	**3,274**

For the purpose of expanding the marketing of networking products in Mainland China, Alpha invested $16,985 thousand in TGC, Inc. in September 2004. As of December 31, 2007, the Company had obtained 1.83% of the voting shares.

For the purpose of new products testing and certification, Alpha invested $9,996 thousand in QuieTek Corp. in April 2007. As of December 31, 2007, the Company had obtained 3.64% of the voting shares.

The stock of the Company's investees TGC, Inc. and QuieTek Corp. is not traded publicly, and therefore, the cost method is used to measure its value. In addition, TGC Inc. had net losses for the past years including the current year, and as a result, the Company recognized $16,985 thousand of impairment loss.

6. Derivative financial instruments

As of December 31, 2007 and 2006, the Company used derivative financial instruments to hedge existing assets and liabilities denominated in foreign currency, was summarized below:

(i) Derivative financial assets

Contract	December 31, 2007 Notional amount (in thousands)	Maturity	Carrying amount
Call option (sell USD)	USD10,000	2008.01	(102)
Put option (sell USD)	USD10,000	2008.01	(429)
Put option (buy USD)	USD10,000	2008.01	1,041
			$ 510

Contract	December 31, 2006 Notional amount (in thousands)	Maturity	Carrying amount
Put option (sell USD)	USD50,000	2007.01	206
Call option (sell USD)	USD30,000	2007.01	(568)
Put option (buy USD)	USD35,000	2007.01	1,306
			$ 944

The above derivative financial instruments are classified under financial assets at fair value through profit or loss－current.

(ii) Derivative financial liabilities

Contract	December 31, 2007 Notional amount (in thousands)	Maturity	Carrying amount
Cross currency swap contract	$ USD75,000	2008.01	$ 13,460

(Continued)

	December 31, 2006		
Contract	**Notional amount (in thousands)**	**Maturity**	**Carrying amount**
Forward foreign currency exchange	$ USD10,000	2007.01	2,527
Cross currency swap contract	USD20,000	2007.01	6,250
			$ 8,777

The above derivative financial instruments are classified under financial liabilities at fair value through profit or loss－current.

(iii) Embedded non-equity derivative

	December31, 2007	December31, 2006
Embedded non-equity derivative	$ -	17,508

The above derivative financial instruments are classified under financial liabilities at fair value through profit or loss－noncurrent and disclosed in note 15.

7. Notes and Accounts Receivable, Net

	December31, 2007	December31, 2006
Notes receivable	$ 132,649	-
Accounts receivable	2,465,935	2,379,038
Less: allowance for doubtful accounts	(13,368)	(11,289)
	$ 2,585,216	2,367,749

8. Inventories

	December31, 2007	December31, 2006
Finished goods	$ 376,192	285,380
Work in process	525,828	477,363
Raw materials	1,440,291	1,455,629
	2,342,311	2,218,372
Less: Provision for devaluation	(197,689)	(155,149)
	$ 2,144,622	2,063,223

(Continued)

9. Short-term Borrowings

Short-term borrowings consisted of the following as of December 31, 2007 and 2006:

	2007		2006	
	Amount	**Rate %**	**Amount**	**Rate %**
Loan for purchasing materials	$ -	-	627,473	5.87%~5.9729%
Unsecured borrowings	102,564	5.832%~5.85%	33,376	0.58%
	$ 102,564		660,849	
Unused credit facilities	$ 4,015,765		5,059,171	

10. Bonds payable

Alpha issued unsecured convertible bonds totaling $1,200,000 thousand on January 5, 2006, with duration of 5 years and a coupon rate of zero. The conversion price was $37 (New Taiwan dollars) per share when the bonds were issued. On December 31, 2007, the conversion price was adjusted to $28.97 (New Taiwan dollars) per share based on the prescribed formula. In addition, the bondholders may exercise their conversion options at any time during the period from one month after the issuance date to ten days before the maturity date, by converting the bonds into Alpha's common stock. The bondholders may redeem their bonds after the issuance date, at a redemption price of the par value of the bonds. Based on SFAS 36, Alpha separated the conversion option from the liability elements when the convertible bonds were issued and recorded them as equity and liability, respectively. Details are summarized as follows:

Item	
Total amount of convertible bonds	$ 1,200,000
Fair value of non-equity embedded derivatives	(32,640)
Issue cost	(5,639)
Fair value of convertible bonds	(1,048,081)
Equity element – conversion options	$ 113,640

The above straight bond has an effective interest rate 2.6%.

As of December 31, 2007 and 2006, the fair values of the above non-equity embedded derivatives estimated based on an evaluation method amounted to $0 thousand and $17,508 thousand, respectively.

(Continued)

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

As of December 31, 2007, unsecured convertible bonds amounting to $777,100 thousand had been converted into 25,653 thousand shares of Alpha's common stock (of which 2,547 thousand shares were still in the process of subscription, recorded under Advance Receipts for Common Stock). The bonds conversion above increased capital surplus by $526,154 thousand.

The details of convertible bonds as December 31, 2007 and 2006, are summarized below:

	2007	2006
Convertible bonds payable	$ 1,200,000	1,200,000
Less: Unamortized discount	(33,419)	(123,066)
Converted into common stock	(777,100)	-
Current portion	(389,481)	-
	$ -	1,076,934

11. Retirement Plans

The following table sets forth the benefit obligation and accrued pension balance for the defined benefit plan as of December 31, 2007 and 2006:

	2007	2006
Benefit obligation:		
Nonvested benefit obligation	$ (298,398)	(287,561)
Vested benefit obligation	-	-
Accumulated benefit obligation	(298,398)	(287,561)
Projected future salary increase	(255,324)	(175,956)
Projected benefit obligation	(553,722)	(463,517)
Fair value of plan assets	309,328	287,970
Funded status	(244,394)	(175,547)
Unrecognized net loss	171,262	104,366
Accrued pension cost	$ (73,132)	(71,181)

On October 1, 2006, Alpha recognized the accrued pension cost amounting to NT$9,148 thousand from assuming the projected benefit obligation in excess of the plan assets of Cellvision from the merger.

(Continued)

The components of net periodic pension cost for 2007 and 2006 are summarized as follows:

		2007	2006
The defined benefit plan:			
Service cost	$	13,665	12,437
Interest expenses		12,720	12,361
Actual returns on pension fund		(8,640)	(6,784)
Amortization		3,624	(2,634)
Net pension cost	$	21,369	15,380
The defined contribution plan:	$	70,345	46,533

Actuarial assumptions at December 31, 2007 and 2006, are summarized as follows:

	2007	2006
Discount rate	2.75%	2.75%
Rate of increase in future compensation levels	4.00%	3.00%
Expected long-term rate of return on plan assets	2.75%	2.75%

12. Stockholders' Equity

(1) Common stock

Pursuant to a stockholders' resolution on June 9, 2006, Alpha increased its common stock by $405,161 thousand through the transfer of unappropriated earnings, capital surplus and employees' bonuses of $116,064 thousand, $174,097 thousand and $115,000 thousand respectively. The capital increase was registered with the governmental authorities.

Based on the resolution of Alpha's board of directors on September 22, 2006, Alpha issued 21,780 thousand shares to acquire Cellvision. This was approved by the Securities and Futures Bureau (SFB) and registered with the governmental authorities.

Pursuant to a stockholders' resolution on June 8, 2007, Alpha augmented the authorized common stock to $6,600,000 thousand, and increased its common stock by $224,776 through the transfer of unappropriated earnings and employees' bonuses of $107,776 thousand and $117,000 thousand, respectively. The capital increase was registered with the governmental authorities.

(Continued)

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(2) Employee stock options

As of December 31, 2006, employee stock options issued were as follows:

Classification	Issue date	Issued units in thousands	Option duration	Exercised period	Exercise price per share (NT$)
First issuance of employee stock options in 2004	Jan. 1, 2004	29,720	Jan. 1, 2004~ Dec. 31, 2009	Jan. 1, 2006~ Dec. 31, 2009	10.00
Second issuance of employee stock options in 2004	Jan. 30, 2004	80	Jan. 30, 2004~ Jan. 29, 2010	Jan. 30, 2006~ Jan. 29, 2010	10.00
First issuance of Employee stock options in 2007	Oct. 5, 2007	15,000	Oct. 5, 2007~ Oct. 4, 2012	Oct. 5, 2009~ Oct. 4, 2012	38.50
Second issuance of employee stock options in 2007	Nov. 9, 2007	7,500	Nov. 9, 2007~ Nov. 8, 2012	Nov. 9, 2009~ Nov. 8, 2012	32.30
Second issuance of employee stock options in 2007	Dec. 6, 2007	7500	Dec. 6, 2007~ Dec. 5, 2012	Dec. 6, 2009~ Dec. 5, 2012	30.75

On July 29, 2006, the exercise price per share of employee stock options issued in 2004 was adjusted from NT$12.4 to NT$10 in accordance with the plan. In 2006, 10,241 thousand shares of Alpha's employee stock options were exercised, and $125,320 thousand had been received as of December 31, 2006.

In 2007, 8,036 thousand shares of Alpha's employee stock options were exercised, and $80,360 thousand had been received as of December 31, 2007. Of those shares, 2,769 thousand shares were still in the subscription process, recorded under advance receipts for common stock.

Alpha applied the intrinsic value method in accounting for stock options granted to employees after the year 2004 under the stock option plan. Under the intrinsic value method, no compensation cost was recognized since the exercise price of Alpha's employee stock options was equal to the market price of the underlying stock on the date of the grant.

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If the compensation cost of employee stock options were accounted for by using the fair-value method and the Black-Scholes model is used to estimate the fair value of employee stock options granted, the fair value of each unit of employee stock options would be $0.6~10.3. Weighted-average assumptions are summarized as follows:

Expected dividend yield	15%
Expected volatility	37.16%~45.24%
Risk-free interest rate	1.98%~2%
Expected life	5~6 years

Information related to Alpha's employee stock option plan for the years ended December 31, 2007 and 2006, is as follows:

	2007		2006	
Employee stock option	**Options (thousands)**	**Weighted-average exercise price (NT$)**	**Options (thousands)**	**Weighted-average exercise price (NT$)**
Outstanding at beginning of year	18,411	10.00	28,652	12.40
Granted	30,000	35.01	-	-
Exercised	(8,036)	10.00	(10,241)	12.24
Forfeited	-	-	-	-
Outstanding at end of year	40,375	28.60	18,411	10.00
Exercisable at end of year	40,375		18,411	
Weighted-average fair value of options granted during the year (NT$)	$ 0.6~10.3		0.6	

If the fair-value method for the compensatory employee stock option plan is adopted, the pro forma net income and earnings per common share on the accompanying consolidated financial statements would be as follows:

		2007	2006
Net income	Net income	$ 1,293,744	1,048,396
	Pro forma net income	1,277,963	1,046,926
Basic earnings per common share	Earnings per common share (NT$)	3.26	3.10
	Pro forma earnings per common share (NT$)	3.22	3.10
Diluted earnings per common share	Earnings per common share (NT$)	3.02	2.79
	Pro forma earnings per common share (NT$)	2.99	2.79

(Continued)

As of December 31, 2007 and 2006, the authorized common stock amounted to $6,600,000 thousand (including $500,000 thousand authorized for the issuance of the employee stock options) and $5,000,000 thousand (including $300,000 thousand authorized for the issuance of the employee stock options), respectively, and the issued and outstanding common stock was 406,287 thousand shares and 355,437 thousand shares, respectively, at a par value of ten New Taiwan dollars.

(3) Capital surplus

Capital surplus consisted of the following as of December 31, 2007 and 2006:

	2007	2006
Issuance of new shares – premium	$ 1,482,932	956,778
Conversion options of convertible bonds (note 10)	40,049	113,640
	$ 1,522,981	1,070,418

Pursuant to the ROC Company Act, realized capital surplus can be used to increase share capital after offsetting accumulated deficit. Realized capital surplus includes proceeds received in excess of the par value of common stock issued and any amounts donated to the company.

(4) Legal reserve

According to the ROC Company Act, 10 percent of the annual earnings shall be allocated as legal reserve until accumulated legal reserve equals the issued common stock. Legal reserve can only be used to offset accumulated deficits and increase common stock.

(5) Distribution of earnings and dividend policy

After paying income tax, offsetting any accumulated deficit, and appropriating 10% of the balance as legal reserve, the balance may be distributed in the following order in accordance with Alpha's articles of incorporation: 2% as remuneration to directors and supervisors and 10%~22.5% as employee bonuses. The distribution of employee bonuses could include the employees of Alpha's subsidiaries. An additional reserve on certain earnings may also be retained. The distribution of the remaining earnings together with prior years' unapproriated earnings could be proposed by the board of directors and approved of the shareholders' meeting.

(Continued)

Alpha has adopted the remaining dividend policy after considering the industry environment, business growth characteristics, long-term financial plan, retention of talent and long-term operation of the business. Alpha considers the capital budget to determine the distribution of stock dividends, accompanied by cash dividends which should be no less than 10% of total dividends.

According to ROC SFB regulations, a publicly listed company should retain a special reserve equal to any deductions made from stockholders' equity related to items such as foreign currency translation adjustments before distribution of earnings. If the aforementioned deduction from stockholders' equity is reversed, the same amount could be removed from special reserve and transferred to unappropriated earnings.

Information about Alpha's directors' and supervisors' remuneration and employees' bonuses which were distributed from unappropriated earnings of 2006 is as follows:

Employees' bonuses—cash	$ 945
Employees' bonuses—stock	117,000
Directors' and supervisors' remuneration	18,871
	$ 136,816

Alpha had distributed employees' stock bonuses constituting 3.29% of its outstanding shares as of December 31, 2006. Assuming that employees' bonuses and directors' and supervisors' remuneration were recognized as periodic expenses, net income per common share for 2006 would be adjusted to $2.70 (New Taiwan dollars).

The actual distribution of employees' bonuses and directors' and supervisors' remuneration for 2007 is subject to the proposal of the board of directors and a resolution of the stockholders. Relevant information would be available on the Market Observation Post System of the Taiwan Stock Exchange after the above-mentioned meetings.

13. Income Taxes

(1) The income tax return of each consolidated entity is filed separately and could not be consolidated with Alpha's filing. Alpha and it subsidiaries are subject to the current tax rate of the countries in which they operate. Alpha Holding, Alpha Global, Des Voeux and Alpha Investment are exempt from taxes.

The statutory income tax rate of consolidated entities established in Taiwan is 25%. The ROC government enacted the Income Basic Tax Act ("IBTA"), which is effective from January 1, 2006.

(Continued)

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

For the years ended December 31, 2007 and 2006, income tax expense was as follows:

		2007	2006
Current	$	251,312	251,140
Deferred		2,843	(2,395)
Additional 10% income surtax on undistributed earnings		8,823	25,910
	$	262,978	274,655

(2) The reconciliation of the expected income tax expense at the statutory tax rate and the actual income tax expense for the years ended December 31, 2007 and 2006, was as follows:

		2007	2006
Income tax expense computed at the statutory tax rate	$	405,958	343,741
Tax effect of permanent difference		9,383	(4,628)
Investment tax credits		(243,797)	(180,123)
Additional 10% surtax on undistributed earnings		8,823	25,910
Valuation allowance for deferred tax assets		40,279	45,915
Prior year's adjustment		42,332	43,840
Income tax expense	$	262,978	274,655

(3) The components of deferred income tax assets (liabilities) as of December 31, 2007 and 2006, are summarized as follows:

		2007	2006
Deferred tax assets—current:			
Investment tax credits	$	25,000	38,129
Employee benefits		1,500	1,500
Unrealized decline in value of inventories		48,549	38,768
Product warranty		51,479	76,533
Others		18,368	8,535
		144,896	163,465
Less: valuation allowance		(122,109)	(125,000)
	$	22,787	38,465

(Continued)

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

		2007	2006
Deferred tax assets—non-current:			
Investment tax credits	$	136,779	62,357
Loss carryforward		25	11,746
Accrued pension cost		18,283	17,968
Investment loss on long-term equity investments in foreign entities		56,488	50,686
Employee benefits		2,625	3,000
Goodwill		(8,430)	(1,687)
Foreign currency translation adjustment		(37,102)	(18,843)
		168,668	125,227
Less: valuation allowance		(167,925)	(124,746)
	$	743	481
Total deferred tax asset	$	359,887	309,222
Total deferred tax liabilities	$	45,532	20,530
Total valuation allowance	$	290,825	249,746

(4) The Company's investment credits from the purchase of machinery, research and development expenditure, and training expenditure under the ROC Statute for Upgrading Industries that can be utilized each year are limited to 50 percent of the year's current tax expense. However, the foregoing limit does not apply to the last year of the investment tax credits' expiration period.

According to the Merger Law, Alpha, after merging with Cellvision, is entitled to the tax credit for investment in the amount of $13,129 thousand.

As of December 31, 2007, Alpha's unused investment tax credits and related expiration dates were as follows:

Unused investment tax credit	Expiration year
$ 22,114	2008
12,776	2009
28,000	2010
98,889	2011
$ 161,779	

(5) As of the December 31, 2007, Alpha's income tax returns had been examined by the tax authorities through 2005. However, due to different interpretations of investment credit for research and development, Cellvision's income tax returns for the years from 2002 to 2006 were assessed additional tax amounting to $38,182 thousand. Alpha did not agree with the assessment and filed appeals. The expected related liability was accrued in the consolidated financial statements. As of December 31, 2007, no responses from the tax authorities with regard to the appeals had been received.

(Continued)

(6) According to the ROC Income Tax Act, losses of ROC subsidiaries as assessed by the tax authorities can be carried forward to offset the future 5 years' taxable profits. As of December 31, 2007, the unused loss carryforwards and related expiration years of Net Mag and Aescu were as follows:

Year of loss	Tax effect	Expiration years
2007	$ 25	2012

(7) Information relating to the ICA of Alpha as of December 31, 2007 and 2006, is summarized as follows:

	2007	2006
Unappropriated earnings:		
Earned after December 31, 1997	$ 1,870,227	1,536,633
ICA balance	$ 239,202	145,967
Expected creditable ratio for earnings distribution to resident stockholders	23.2.% (estimated)	19.34% (actual)

14. Net Income per Common Share

	2007		2006	
	Before taxes	After taxes	Before taxes	After taxes
Basic net income per common share:				
Income before cumulative effect of changes in accounting principle	$ 1,534,317	1,293,758	1,307,606	1,034,882
Cumulative effect of changes in accounting principle	-	-	15,445	13,514
Net income	$ 1,534,317	1,293,758	1,323,051	1,048,396
Weighted-average common shares outstanding (thousand shares)	396,296	396,296	337,923	337,923
Basic net income per common share (NT$)	$ 3.87	3.26	3.92	3.10

(Continued)

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

	2007 Before taxes	2007 After taxes	2006 Before taxes	2006 After taxes
Diluted net income per common share:				
Net income	$ 1,534,317	1,293,758	1,323,051	1,048,396
Potential dilution effects of common shares －convertible bonds	21,638	16,229	28,853	21,640
Net income when calculating diluted EPS	**$ 1,555,955**	**1,309,987**	**1,351,904**	**1,070,036**
Weighted-average common shares outstanding (thousand shares)	396,296	396,296	337,923	337,923
Employee stock options assumed exercised at beginning of year (in thousand shares)	9,877	9,877	6,082	6,082
Convertible bonds assumed converted at the time of issuance (in thousand shares)	27,265	27,265	38,961	38,961
Diluted weighted-average common shares outstanding (thousand shares)	**433,438**	**433,438**	**382,966**	**382,966**
Diluted net income per common share (NT$)	**$ 3.59**	**3.02**	**3.53**	**2.79**

15. Financial Instruments

(1) Derivative financial instruments

The Company’s transactions involving 2007 and 2006 derivative financial instruments are disclosed in note 6.

(2) Non-derivative financial instruments

(i) The Company’s non-derivative financial assets or liabilities with short-term maturities include notes and accounts receivable, other financial assets－current/noncurrent, short-term borrowings, and accounts payable, whose fair value was estimated based on book value at the balance sheet date. The carrying amounts approximate their fair value due to the short-term nature of these items.

(Continued)

(ii) Except for the financial assets and liabilities identified in (i) description, the carrying amounts and estimated fair value of financial instruments as of December 31, 2007 and 2006, were as follows:

		December 31,		
	2007		2006	
	Book value	Fair value	Book value	Fair value
Financial assets:				
Available-for-sale financial assets – noncurrent	$ 57,300	57,300	-	-
Financial assets carried at cost – noncurrent	9,996	3(ii) below	3,274	3(ii) below
Financial liabilities:				
Bonds payable (including current portion)	389,481	389,481	1,076,934	1,076,934

(3) The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

(i) The fair value of bonds payable, available-for-sale financial assets, and financial assets (liabilities) at fair value through profit or loss is the active market quoted price if it is available. If the market price is unavailable, the Company will determine the fair value based on an evaluation method, and the estimates and assumptions incorporated in such evaluation are consistent with those used by market participants in their pricing of financial instruments.

(ii) It is not practicable to determine the fair values of financial assets carried at cost when these investments are not publicly traded. Refer to note 5 for the details.

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(4) Details of quoted market prices and estimated fair values of financial instruments are as follows:

	December 31,			
	2007		2006	
	Quoted market price	Estimated fair value	Quoted market price	Estimated fair value
Financial assets:				
Cash and cash equivalents	3,135,406	-	3,097,024	-
Notes and accounts receivable (including related parties)	-	5,670,505	-	5,087,307
Available-for-sale financial assets – non-current	57,300	-	-	-
Financial assets at fair value through profit or loss – current	-	510	-	944
Other financial assets – current	-	32,356	-	15,403
Other financial assets – noncurrent	-	36,187	-	32,711
Financial liabilities:	-		-	
Short-term borrowings	-	102,564	-	660,849
Accounts payable (including related parties)	-	3,686,653	-	3,331,476
Financial liabilities at fair value through profit or loss – current	-	13,460	-	8,777
Financial liabilities at fair value through profit or loss – non-current	-	-	-	17,508
Bonds payable (including current portion)	-	389,481	-	1,076,934

(5) Net gain on valuation of financial assets (liabilities) resulting from the changes in fair value amounted to $4,558 thousand and $16,259 thousand for the years ended December 31, 2007 and 2006, respectively.

(Continued)

(6) Financial risk information

(i) Market price risk

As the Company and subsidiaries' derivative financial instruments are for hedging purposes, the gains or losses due to changes in the interest rates or foreign exchange rates will be naturally offset by the hedged items. As a result, market price risk is considered low. Publicly traded stocks held by the Company are classified as available-for-sale financial assets. Since these assets are measured by the fair value, the Company and subsidiaries will be exposed to the risks of equity market price change.

(ii) Credit risk

The Company's potential credit risk is derived primarily from cash and cash equivalents, and accounts receivable. The Company and subsidiaries maintain their cash in various creditworthy financial institutions. Credit risk exposure to each financial institution is controlled by the Company. As a result, the Company believes that there is no concentration of credit risk of cash.

The main customers of the Company and subsidiaries lie in the networking and related industries. It is a normal practice for the Company and subsidiaries to provide customers a credit limit according to their credit evaluations. Therefore, the credit risk of the Company and subsidiaries is mainly influenced by the networking industry.

However, the main customers of the Company and subsidiaries are multinational companies or companies with good credit ratings. From time to time, the Company and subsidiaries monitor customers' credit conditions and hence have never encountered any significant loss due to credit risk. As of December 31, 2007, 70% of the Company's accounts receivable were for a group of five customers.

Although, there is a potential for concentration of credit risk, the Company and subsidiaries routinely assess the collectibility of the accounts receivable and make a corresponding allowance for doubtful accounts. The management does not foresee any significant loss for the Company and subsidiaries.

(iii) Liquidity risk

There is no liquidity risk of being unable to raise capital to settle contract obligations since the Company and subsidiaries have sufficient capital and working capital to fulfill the contract obligations.

(Continued)

Liquidity risk is the risk of being unable to settle derivative contracts on schedule. The purpose of these instruments held by the Company and subsidiaries was to manage and hedge the floating interest rates and foreign currency exchange rates. There is no significant liquidity risk for the related cash flows. The Company and subsidiaries have liquidity risk when investing in financial assets carried at cost that are not publicly traded.

16. Related-party Transactions

(1) The name and relationship of the related parties with which Alpha and its subsidiaries had significant transactions are shown below:

Name	Relationship
D-Link Corporation (D-Link)	Parent of Alpha (After March 2007, it became the largest shareholder.)
D-Link System Inc. (DLSI)	Subsidiary of D-Link
Xtramus Technologies (XT)	Subsidiary of D-Link
Bothhand Enterprise Inc. (BEI)	Investee of D-Link accounted for under the equity method
D-Link International Pte Ltd. (DIPL)	Subsidiary of D-Link

(2) Significant transactions with related parties as of and for the years ended December 31, 2007 and 2006, are summarized as follows:

(a) Sales

	2007		2006	
	Amount	Percentage of net sales	Amount	Percentage of net sales
DIPL	$ 8,855,068	39	6,912,260	32
D-Link	811,444	4	1,723,034	8
DLSI	643,391	3	1,039,699	5
Others	195,483	1	20,480	-
	$ 10,505,386	47	9,695,473	45

(Continued)

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

As of December 31, 2007 and 2006, receivables resulting from the above transactions were as follows:

	December 31, 2007		December 31, 2006	
	Amount	Percentage of total receivables	Amount	Percentage of total receivables
DIPL	$ 2,640,399	46	2,113,739	42
D-Link	336,935	6	160,435	3
DLSI	3,697	-	430,923	8
Others	123,578	2	13,568	-
Less: allowance for sales returns and discounts	(19,320)	-	-	-
	$ 3,085,289	54	2,718,665	53

The collection terms for sales to unrelated customers and related parties were 30 to 75 days and 45 to 90 days, respectively. However, collection terms for related parties might be further extended when necessary.

The amount that Alpha paid or received from D-Link was settled by the receivables due from and the payables due to D-Link.

As of December 31, 2007 and 2006, accounts receivable from related parties outstanding over 90 days were classified to other financial assets – current as follows:

	December31, 2007	December31, 2006
D-Link	$ -	8,409

(b) Purchases

	2007		2006	
	Amount	Percentage of net purchases	Amount	Percentage of net purchases
BEI	$ 197,567	1	179,252	1
Others	9,043	-	32,043	-
	$ 206,610	1	211,295	1

ALPHA NETWORKS INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

There are no significant differences in payment terms between related parties and third-party suppliers. The payment terms were both 30 to 90 days.

As of December 31, 2007 and 2006, payables resulting from the above purchases were as follows:

		December 31, 2007		December 31, 2006	
		Amount	Percentage of total purchases	Amount	Percentage of total purchases
Accounts payable:					
BEI	$	51,484	1	54,769	2
Others		392	-	202	-
	$	51,876	1	54,971	2

(c) Service fees and others

The Company and subsidiaries paid fees to related parties for warranty services, royalties, and other services. The total fees for the years ended December 31, 2007 and 2006, and the related unpaid balance as of December 31, 2007 and 2006, are summarized as follows:

		2007		2006	
		Current expense	Accrued expense	Current expense	Accrued expense
DIPL	$	25,447	10,203	24,749	8,628
D-Link		23,420	12,842	19,456	12,600
Others		14,501	2,146	8,698	1,781
	$	63,368	25,191	52,903	23,009

(d) Acquisition / disposal of property, plant and equipment

(i) Acquisition of property, plant and equipment for the years ended December 31, 2007 and 2006, and the related unpaid balance as of December 31, 2007 and 2006, are summarized as follows:

		2007		2006	
		Amount	Account payable	Amount	Account payable
XT	$	16,751	-	23,779	-
Others		4,139	494	1,520	210
	$	20,890	494	25,299	210

(Continued)

(ii) Disposal of equipment for the years ended December 31, 2007 and 2006, and the receivables as of December 31, 2007 and 2006, are summarized as follows:

	2007		2006	
	Amount	**Account receivable**	**Amount**	**Account receivable**
XT	$ -	-	850	893

As of December 31, 2007 and 2006, the unrealized inter-company profits resulting from property, plant and equipment transactions amounted to $160 thousand and $215 thousand, respectively, and were recorded as deferred credit.

(e) Others

(i) As of December 31, 2007 and 2006, net payable to related parties resulting from certain payments made by the Company and subsidiaries on behalf of related parties or made by related parties on behalf of the Company and subsidiaries were as follows:

	2007	2006
D-Link	$ 3,943	-
Others	404	-
	$ 4,347	-

(ii) Alpha entered into a plant lease agreement with D-Link for the plant located in the Hsin Chu Science Park and the Taipei Neihu office. The rental expenses amounted to $12,906 thousand and $6,934 thousand in 2007 and 2006, respectively. As December 31, 2007 and 2006, payable resulting from the above transactions amounted to $1,399 thousand and $3,753, respectively, which were recorded in payable to related parties.

17. Pledged Assets

Assets pledged as collateral as of December 31, 2007 and 2006, are summarized as follows:

Pledged assets	Pledged to secure	2007	2006
Time deposit (recorded in other financial assets – noncurrent)	Import guarantee for Customs	$ 15,500	15,500

18. Commitments and Contingencies

(1) Operating leases

	Lesser	Period for lease	Rental expense in 2007	Payment method
Land	Hsinchu Science Park	Nov. 2003~Dec. 2022	$7,685 thousand	Monthly

According to the lease agreement, rent payment is subject to an adjustment as the government adjusts the land value.

(2) As of December 31, 2007 and 2006, Alpha had outstanding letters of credit amounting to $0 thousand and $3,008 thousand, respectively.

(3) Alpha entered into royalty agreements with Fine Point, Wind River, and others. Pursuant with the terms of each signed agreement, Alpha is obligated to pay royalties when Alpha's products applied technologies specified in the royalty agreements. Total royalty expenses incurred under these agreements for the years ended December 31, 2007 and 2006, amounted to $17,747 thousand and $9,876 thousand, respectively.

19. Other Information

(1) The information on personnel, depreciation, and amortization expenses by function for the years ended December 31, 2007 and 2006, is summarized as follows:

	2007			2006		
Account	**Cost of goods sold**	**Operating expense**	**Total**	**Cost of goods sold**	**Operating expense**	**Total**
Personnel expenses:						
Salaries	$ 841,172	1,075,553	1,916,725	646,003	757,449	1,403,452
Labor and health insurance	32,434	77,575	110,009	25,338	58,613	83,951
Pension	25,077	66,503	91,580	21,903	40,010	61,913
Others	35,026	74,364	109,390	24,922	79,084	104,006
Depreciation	155,645	212,546	368,191	145,708	195,781	341,489
Amortization	57	70,644	70,701	243	66,731	66,974

(Continued)

(2) Business combination

On April 17, 2006, Alpha's board of directors approved the proposal to merge with Cellvision. Alpha was the surviving corporation. In accordance with the agreement and considering Alpha's and Cellvision's retained earnings, the merger was consummated through the issuance of 21,780 thousand new common shares, par value NT$10 per share, in exchange for all of the outstanding common shares of Cellvision, representing an exchange ratio of 1.8 shares of common stock of Cellvision to one share of common stock of Alpha.

The merger was accounted for in accordance with ROC SFAS No. 25 "Business Combinations" using the purchase method of accounting. Under the purchase method, the aggregate purchase price was determined based on the market value of shares issued as of the acquisition date. The market value of shares issued and direct transaction cost amounted to NT$745,993 thousand. The market value of shares issued was determined based on the average market price of Alpha's common shares over a reasonable period before and after the terms of the acquisitions were agreed upon and announced on April 17, 2006. The excess purchase price over the value of the net identifiable tangible and intangible assets was recorded as goodwill. The fair value assigned to tangible and intangible assets acquired and liabilities assumed is based on estimates and assumptions of management.

The following represents the allocation of the purchase price to the acquired net assets of Cellvision on October 1, 2007:

Purchase price	$	745,993
Current assets	673,500	
Property, plant and equipment	20,461	
Intangible assets	57,563	
Other assets	4,894	
Current liabilities	(145,308)	
Fair value of net assets		$ 611,110
Goodwill		$ 134,883

As of December 31, 2007, there were no events or circumstances indicating possible impairment.

The following unaudited pro forma financial information summarizes the combined results of operations of Alpha and Cellvision as though the business combination had taken place on January 1, 2006.

	December 31 2006
Net sales	$ 22,227,773
Cost of goods sold	18,515,996
Gross profit	3,711,777
Operating expenses	2,111,669
Net income	1,142,651
Basic earnings per share	3.23

20. Segment Financial Information

(1) Industry information

The Company principally operates in one industry segment: research, development, manufacturing and sale of network communication products.

(2) Geographic information

2007	Asia	Americas	Adjustments and eliminations	Consolidated
Area revenue:				
Third-party customers	$ 22,351,430	-	-	22,351,430
Inter-company	982,640	102,701	(1,085,341)	-
	$ 23,334,070	102,701	(1,085,341)	22,351,430
Operating income	$ 1,493,753	7,713	55,256	1,556,722
Area identifiable assets	$ 17,668,795	53,400	(4,037,046)	13,685,149

2006	Asia	Americas	Adjustments and eliminations	Consolidated
Area revenue:				
Third-party customers	$ 21,469,154	-	-	21,469,154
Inter-company	1,898,860	100,073	(1,998,933)	-
	$ 23,368,014	100,073	(1,998,933)	21,469,154
Operating income	$ 1,038,719	4,764	264,123	1,307,606
Area identifiable assets	$ 116,248,718	24,668	(3,456,228)	12,817,158

(Continued)

(3) Export sales

The export sales of the consolidated entities located in the ROC for the years ended December 31, 2007 and 2006, are summarized as follows:

	2007		2006	
	Amount	**Percentage of net sales**	**Amount**	**Percentage of net sales**
Asia	$ 6,229,176	30	6,298,657	30
Americas	8,067,117	39	5,007,456	24
Europe	5,417,452	25	5,549,700	27
Others	748,892	4	1,271,562	6
	$ 20,462,637	**98**	**18,127,375**	**87**

(4) Major customers

Individual customers that represented greater than 10% of consolidated revenue in 2007 and 2006 were as follows:

	2007		2006	
	Amount	**Percentage of net sales**	**Amount**	**Percentage of net sales**
DIPL	$ 8,855,068	39	6,912,260	32
Huawei Technologies Co., Ltd.	2,172,298	10	1,834,674	9
	$ 11,027,366	**49**	**8,746,934**	**41**