

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549  
FORM 20-F

(Mark One)

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

or

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2016

or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

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: 0-30910

O<sub>2</sub>MICRO INTERNATIONAL LIMITED  
(Exact Name of Registrant as Specified in Its Charter)

The Cayman Islands  
(Jurisdiction of Incorporation or Organization)

Grand Pavilion Commercial Centre, West Bay Road  
P.O. Box 32331 Grand Cayman KY1-1209, Cayman Islands  
(Address of Principal Executive Offices)

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

<u>Title of Each Class</u>	<u>Name of Each Exchange On Which Registered</u>
American Depositary Shares Ordinary Shares, par value \$0.00002 per share	NASDAQ Global Select Market Cayman Islands Stock Exchange

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

None  
(Title of Class)

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

None  
(Title of Class)

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.

As of December 31, 2016, there were 1,279,124,900 ordinary shares, par value US\$0.00002 per share, outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

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  No

Note – Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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.

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

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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

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

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  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 Exchange Act).

Yes  No

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Signatures

## Certain Definitions and Conventions

In this Annual Report on Form 20-F (“Annual Report”), references to “\$” and “dollars” are to United States dollars. Percentages and certain amounts contained herein have been rounded for ease of presentation. Any discrepancies in any table between totals and the sums of amounts listed are due to rounding.

### SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains statements of a forward-looking nature. These statements are made under the “safe harbor” provisions of the U.S. Private Securities Litigation Reform Act of 1995. You can identify these forward-looking statements by terminology such as “may,” “will,” “expects,” “should,” “could,” “plans,” “intends,” “anticipates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these terms and other comparable terminology. These forward-looking statements include, without limitation, statements regarding the following: our expectation to target and design products for specific applications; to increase expenses for personnel and new product development; to protect our technology and to expand our product offerings; our anticipation that sales to a relatively small number of customers will continue to account for significant portion of net sales; our expectation that we will no longer need to reduce costs and reduce our personnel our expectation that non-U.S. operations and sales will recover and continue to account for a substantial percentage of our net sales; our expectation to return to profitably and/or cash flow break even in the near future; our expectation that competition for qualified personnel will remain intense; our expectation that we will continue to incur substantial legal expenses that may vary with the level of activity in legal proceedings at any given point in time; our statements regarding the growing popularity of thinner displays, mobile computing, electric vehicles, more efficient general lighting, and portable devices; our belief that we participate in large and growing markets; our belief that potential future growth in the LED television, mobile computing, general lighting, industrial and automotive markets represents an attractive growth opportunity for us; our belief that the use of cold cathode fluorescent lamps (“CCFL”) is not a significant market for our current business model, our belief that manufacturers are turning to innovative new semiconductor technologies to manage capacity more efficiently; our belief that there is an increasing need for higher levels of system integration; our belief in the need for mixed-signal and analog integrated circuits specifically designed to optimize the power system usage in devices; our belief in the need to use advanced design methodologies to allow manufacturers to achieve rapid time-to-market with their new products; our expectation that our markets will be dominated by a small number of major brand name companies; our belief that the our success depends on our ability to develop and introduce new products selected for design into products in certain markets, our ability to develop and introduce products in a timely manner to meet customer demands; our expectation that analog and mixed-signal circuits have substantially longer life-cycles than digital integrated circuits; our ability to take advantage of cost-efficiencies associated with the “fabless” semiconductor business model; our expectation that our non-U.S. operations will grow and/or non-U.S. sales will continue to account for a substantial percentage of our net sales; our intention is to expand the scope of our global operations; that we expect that our gross profit (loss) (as a percentage of net sales) will continue to fluctuate in the future as a result of the stages of our products in their life cycles; our time expectations and plans to bring the company back to profitability; variations in our product mix; the timing of our product introductions and specific product manufacturing costs; our future gross profits(losses); our expectation that gross margin on products we sell will typically decline over the life of the products; our expectation that gross margin on products will continue at their current and historical levels; our expectation that expenses for personnel and new product development will increase; our expectations regarding the need for future cost reduction measures; our expectation that research and development expenses as a percentage of net sales will continue to fluctuate; our expectation to continue development of innovative technologies and processes, and continued expansion and investment of our engineering, research and development resources; our expectation to continue to invest significant resources into research and development in the future; our expectation that the competition for qualified personnel will remain intense; our expectations regarding the outcome of litigation matters and the effects of such to our company; our belief that the liquidity provided by existing cash, cash equivalents balances and short-term investment will be sufficient to meet our capital requirements for at least the next 12 months; our intention to continue research and development operations; our expectation that semiconductor companies will increasingly be subject to patent infringement and other litigation matters as the number of products and competitors in the semiconductor industry grows; our anticipation that we will not be paying cash dividends in the foreseeable future; our belief that our system-level expertise and extensive experience with power management systems allow us to develop proprietary solutions and foster long-term relationships with our customers; our intention to continue to evaluate additional investment opportunities in our supply chain; our belief that our current facilities are adequate for our needs for the foreseeable future, and that any additional space required will be available to us on commercially reasonable terms; our expectation that our results of operations or cash flows will not be affected to any significant degree by a sudden short-term change in market interest rates; our intention to diversify our customer base and market focus by providing new products used in particular markets; our statements regarding the effect of adoption of certain accounting policies; our expectation that our American Depositary Shares (“ADSs”) will satisfy the “readily tradable” requirement of the trading exchange; our expectation not to become a passive foreign investment company in the future; our intention to use the cash we have raised and conduct our business to reduce the risk of classification as a passive foreign investment company; and our expectation that we will retain our existing primary listing of ADSs on the NASDAQ Global Select Market (“NASDAQ”) in the United States for the foreseeable future. These forward-looking statements are based on our current assumptions and beliefs in light of the information currently available to us. Actual results, levels of activity, performance or achievements may differ materially from those expressed or implied in these forward-looking statements for a variety of reasons, including: changes in demand for devices that use our products; market conditions in the semiconductor industry and the economy as a whole; the stages of our products in their life cycles; variations, expansions or reductions in the mix of our product offerings; the growth and/or contraction of the company; the timing of our product introductions; changes in employment rates; changes in availability and cost of facilities; unpredictability of an inability to control the outcome or timing of litigation; changes in applicable laws or accounting standards; potential delisting of our ordinary shares and/or ADSs from NASDAQ; specific product manufacturing costs; increased competition; changes in laws, rules and regulations regarding our intellectual property; introduction of new competitors or competing technologies; and the increase of unexpected expenses and such other factors discussed under “Key Information - Risk Factors,” “Operating and Financial Review and Prospects” and elsewhere in this Annual Report. We assume no obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise. You are cautioned not to place undue reliance on these forward-looking statements, which apply only as of the date of this Annual Report.

**PART I**

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

See Item 6 below.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

**SELECTED CONSOLIDATED FINANCIAL DATA**

The selected consolidated statements of operations and cash flow data for the years ended December 31, 2016, 2015, and 2014, and the selected consolidated balance sheet data as of December 31, 2016 and 2015, are derived from our audited 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, these consolidated financial statements, including the notes to these consolidated financial statements and “Item 5. Operating and Financial Review and Prospects” as set forth below in this Annual Report. The selected consolidated statements of operations and cash flow data for the years ended December 31, 2013 and 2012 and the selected consolidated balance sheet data as of December 31, 2014, 2013 and 2012, are derived from our audited consolidated financial statements, which are not included in this Annual Report. These consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America.

	<b>Years Ended December 31</b>				
	<b>2016</b>	<b>2015 (as adjusted)</b>	<b>2014 (as adjusted)</b>	<b>2013 (as adjusted)</b>	<b>2012 (as adjusted)</b>
	<i>(in thousands, except per share data)</i>				
<b>Consolidated Statement of Operations Data:</b>					
Net sales	\$ 56,561	\$ 54,841	\$ 63,591	\$ 73,785	\$ 97,666
Cost of sales	27,317	27,145	30,856	36,411	44,067
Gross profit	29,244	27,696	32,735	37,374	53,599
Operating expenses:					
Research and development	15,645	18,493	21,885	27,017	34,310
Selling, general and administrative	19,481	23,632	24,721	30,898	34,594
Costs associated with exit activities	-	-	3,027	-	3,343
Provision for litigation	-	-	-	-	9,422
Litigation income	(23)	-	(75)	-	(100)
Total operating expenses	35,103	42,125	49,558	57,915	81,569
Loss from operations	(5,859)	(14,429)	(16,823)	(20,541)	(27,970)
Non-operating income (loss)— net	3,931	(2,026)	2,950	2,440	2,385
Loss from continuing operations before income tax expense	(1,928)	(16,455)	(13,873)	(18,101)	(25,585)
Income tax expense	1,058	4,640	1,184	992	1,103
Net loss from continuing operations	(2,986)	(21,095)	(15,057)	(19,093)	(26,688)
Income (loss) from discontinued operations, net of tax (3)	-	-	-	(6)	895
Net loss	\$ (2,986)	\$ (21,095)	\$ (15,057)	\$ (19,099)	\$ (25,793)
Basic loss per share:					
Continuing operations	\$ -	\$ (0.02)	\$ (0.01)	\$ (0.01)	\$ (0.02)
Discontinued operations	-	-	-	-	-
	\$ -	\$ (0.02)	\$ (0.01)	\$ (0.01)	\$ (0.02)
Diluted loss per share:					
Continuing operations	\$ -	\$ (0.02)	\$ (0.01)	\$ (0.01)	\$ (0.02)
Discontinued operations	-	-	-	-	-
	\$ -	\$ (0.02)	\$ (0.01)	\$ (0.01)	\$ (0.02)
Shares used to compute basic loss per share: (in thousands)	1,282,141	1,301,465	1,362,465	1,435,778	1,552,190
Shares used to compute diluted loss per share : (in thousands)	1,282,141	1,301,465	1,362,465	1,435,778	1,552,190
Basic loss per ADS (1):					
Continuing operations	\$ (0.12)	\$ (0.81)	\$ (0.55)	\$ (0.67)	\$ (0.86)
Discontinued operations	-	-	-	-	0.03
	\$ (0.12)	\$ (0.81)	\$ (0.55)	\$ (0.67)	\$ (0.83)
Diluted loss per ADS (1):					
Continuing operations	\$ (0.12)	\$ (0.81)	\$ (0.55)	\$ (0.67)	\$ (0.86)
Discontinued operations	-	-	-	-	0.03
	\$ (0.12)	\$ (0.81)	\$ (0.55)	\$ (0.67)	\$ (0.83)

ADS equivalents used to compute basic loss per ADS					
(1):					
(in thousands)	25,643	26,029	27,249	28,716	31,044
ADS equivalents used to compute diluted loss per					
ADS(1):					
(in thousands)	25,643	26,029	27,249	28,716	31,044

	December 31				
	2016	2015	2014	2013	2012
	<i>(in thousands)</i>				
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	\$ 31,332	\$ 41,199	\$ 41,069	\$ 42,293	\$ 27,898
Short-term investments	21,532	11,233	21,481	33,606	69,427
Working capital (2)	61,871	59,904	70,725	84,995	105,448
Total assets	90,689	96,208	116,738	137,419	171,326
Long-term liabilities, excluding current portion (2)	1,294	2,617	761	1,070	10,279
Net assets	80,784	83,117	107,266	126,610	150,372
Ordinary shares and additional paid-in capital	142,771	141,919	141,262	140,231	138,826

- (1) Fifty ordinary shares equal one ADS
- (2) We have classified deferred tax assets and liabilities as noncurrent on the consolidated balance sheets as of December 31, 2016, 2015, 2014, 2013, and 2012 as we have early adopted Accounting Standards Update (“ASU”) 2015-17, Balance Sheet Classification of Deferred Taxes, on a retrospective basis. Prior to the adoption, working capital for the years ended December 31, 2015, 2014, 2013 and 2012 were \$57,724; \$70,623; \$84,990, and \$105,454, respectively. Long-term liabilities were \$411, \$642, \$1,049, and \$10,259, respectively. Please refer to the discussions in note 2 to the consolidated financial statements.
- (3) In November 2010, we initiated shutdown activities of our Network Security Group and therefore, the result of our Network Security Group was reported as discontinued operations in the consolidated financial statements for the years beginning after December 31, 2011. Most of the related shutdown activities were completed in 2011 and we did not have any revenue and expense from the operations of Network Security Group since 2014.



## CAPITALIZATION AND INDEBTEDNESS

Not applicable.

## REASONS FOR THE OFFER AND USE OF PROCEEDS

Not applicable.

## RISK FACTORS

We wish to caution readers that the following important factors, and those important factors described in other reports submitted to, or filed with, the Securities and Exchange Commission, among other factors, could affect our actual results and could cause our actual results to differ materially from those expressed in any forward-looking statements made by us or on our behalf and that such factors may adversely affect our business and financial status and therefore the value of your investment:

### **Global economic and financial, political instability or catastrophes caused or induced by natural disasters could negatively affect our business, results of operations, and financial condition.**

The global economic and financial crisis that has been affecting global business, banking and financial sectors has also been affecting the semiconductor market. Uncertainty in various global markets, economic slowdown in China, and slow recovery in certain economic regions have resulted in sharp declines in electronic products sales from which we generate our income. Current security concerns, political instability in the European Union, economic and political uncertainty in the United States, and financial uncertainty with certain Mediterranean economies, could also negatively affect sales, especially from European customers, and have a negative effect on our supplies of raw goods and materials. The uncertainty in Chinese financial markets could negatively affect our customers' product planning and decrease demand for our products. There could be a number of indirect effects from such turmoil on our business, including, without limitation, the following: significant decreases in orders from our customers; insolvency of key suppliers resulting in product delays; inability of customers to obtain credit to finance purchases of our products and/or customer insolvencies; and counterparty failures negatively impacting our treasury operations. If the effects of the global economic crisis continue unabated, we anticipate our results of operations may be materially and adversely affected. Natural disasters and related catastrophes could also negatively affect our operations. Any natural disaster, economic or financial crisis could cause revenues for the semiconductor industry as a whole to decline dramatically, as the industry as a whole is subject to unexpected change in response to fluctuating global market conditions. Also, if global economic conditions, or the financial condition of our customers, were to deteriorate, additional allowances for uncollectible accounts may be required in the future and such additional allowances would increase our operating expenses and therefore reduce our income from operations and net income. Any serious natural disaster and catastrophes, global economic and financial crisis could materially and adversely affect our results of operations.

### **If the markets for consumer electronics, computers, industrial, communications, or automotive products do not grow substantially or even decrease, our net sales may be harmed.**

Our business focuses on designing, developing and marketing high performance integrated circuits and solutions for manufacturers of products in the consumer electronics, computer, industrial, communications, and automotive markets. As many of the leading sellers of these products have intermediaries to manufacture their products or those portions of their products containing our components, we currently derive the majority of our product revenues from sales to these intermediaries and/or their suppliers. We have targeted, and are designing products for, applications such as LCD and LED monitors, LCD and LED televisions, notebook computers, tablet computers, low/zero emission vehicles, mobile phones, power tools, energy efficient technology relating to sophisticated batteries, LED lighting (both in electronics and in the general lighting sector), and portable electronic equipment, such as camcorders. We believe that the important factors driving growth in these markets include the growing popularity of thinner displays, mobile computing, hybrid and electric vehicles, energy efficient lighting, and portable computing and media devices. In particular, if there is a decline in demand for products using LCDs or LEDs, as well as other devices using our products, or growth for such products is slower than we anticipate, our customers may experience lower demand for their products incorporating our products, which may cause our net sales to suffer. We cannot be certain that the markets for these products will continue to grow. We also cannot be sure that a significant slowdown in these markets will not occur.

### **Fluctuations in our quarterly operating results due to factors such as changes in the demand for electronic devices that utilize our products could adversely affect the trading price of our ADSs.**

If our quarterly operating results fail to meet the expectations of securities analysts, the trading price of our ADSs could be adversely affected, and even trade at below the book value of the Company. Our quarterly operating results have varied substantially in the past and may vary substantially in the future depending upon a number of factors described below and elsewhere in this Risk Factors section, including many factors that are beyond our control. These factors include changes in demand for devices that use our products; market conditions in the highly cyclical semiconductor industry and the economy as a whole; the timing and cancellation of customer orders; the level of orders received that can be shipped in a quarter; the availability of third party semiconductor foundry, assembly and test capacities; fluctuations in manufacturing yields; delays in the introduction of new products; changes in the mix of sales of higher margin products and lower margin products; seasonal changes in demand during the year-end holiday season for devices that use our products; and the amount of legal and other expenses incurred in a particular quarter.

In addition, the trading price of our ADSs may be affected by factors such as: significant price and volume fluctuations in our ADSs and financial markets in the U.S. and other countries, as well as relatively thin trading volume of our ADSs on the NASDAQ Global Select Market and the Cayman Islands Stock Exchange. Further, the trading markets for our ADSs are affected by the research reports that securities or industry analysts publish about us or our business. We do not have control over such coverage. If one or more analysts were to downgrade our ADSs, the price of our ADSs may decline. If one or more analysts cease coverage of our company or does not regularly publish reports on us, we may lose visibility in the financial markets, which could cause the price of our ADSs or trading volume to decline.

**If orders for our products are cancelled or deferred, our net sales, operating margins and net income could be substantially reduced.**

Orders for our products can be cancelled or deferred with little notice from and without significant penalty to our customers. A significant portion of our net sales in any financial reporting period depends on orders booked and shipped in that period. If a large amount of orders placed is cancelled or deferred, our net sales in that period could be substantially reduced. Since we do not have significant non-cancellable backlog, we typically plan our production and inventory levels based on internal forecasts of customer demand, which are highly unpredictable and are often based on a “just in time” inventory system, which can result in substantial fluctuation in ordering and/or last minute changes. In particular, in response to anticipated lengthy lead times, which in the past have been as much as ten weeks or more, to obtain inventory and materials from our suppliers, we place orders with these suppliers in advance of anticipated customer demand, which can result in excess inventory if the expected orders fail to materialize. We also expect to increase our expenses for personnel and new product development. It is difficult for us to reduce our production, inventory, personnel and new product development expenses quickly in response to any shortfalls in net sales resulting from cancelled or deferred orders. As a result, any cancellation or deferral of orders would not only harm our net sales, it would also likely have a disproportionately adverse effect on our operating margins and net income.

**If we do not develop and introduce new products in a timely manner, our net sales and gross margins could be harmed.**

Our success depends upon our ability to develop and introduce new products that our customers in turn select to design into their products in the consumer electronics, computer, industrial, communications, and automotive markets. If we are unable to develop new products in a timely manner, our net sales will suffer. In addition, because our gross margins typically decline over the life cycle of our products as a result of competitive pressures and voluntary pricing arrangements, any failure to develop new products in a timely manner will likely cause our gross margins to decline. The development of our new products is highly complex, and from time to time we have experienced delays in the introduction of new products. Successful product development and introduction of new products depend on a number of factors, including accurate new product definition; timely completion of new product designs; reliance on third party licenses and designers periodically; achievement of manufacturing yields; timely and cost-effective production of new products; delays within our manufacturing foundries; and timely delivery of new third-party supplied products used as key components in devices that incorporate our products. We often incur significant expenditures in the development of a new product without any assurance that it will be selected for design into our customers’ products. If we incur such expenditures for products that are not selected by our customers, our results of operations will be adversely affected and may fluctuate significantly from period to period. Furthermore, even if our products are selected for design into our customers’ products, we cannot be certain that these products will be commercially successful or that we will benefit from any associated sales.

**If we fail to protect our intellectual property rights, competitors may be able to use our technology or trademarks, and this could weaken our competitive position, increase our costs, reduce our margins and reduce our net sales.**

Our success is heavily dependent upon our proprietary technology. We rely primarily on a combination of patent, copyright and trademark laws, trade secrets, confidentiality procedures and contractual provisions to protect our proprietary technology and prevent competitors from using our technology in their products. These laws and procedures provide only limited protection. Our patents may not provide sufficiently broad protection or they may not prove to be enforceable in actions against alleged infringement.

Our ability to sell our products and prevent competitors from misappropriating our proprietary technology and trade names is dependent upon protecting our intellectual property. Despite the precautions we take, unauthorized third parties may copy aspects of our current or future products or obtain and use information that we regard as proprietary. Additionally, our competitors may independently develop similar or superior technology. Policing unauthorized use of patents, software, circuit design or semiconductor design is difficult and some countries’ laws do not adequately protect our proprietary rights to the same extent as the laws of the United States, China and other developed countries. We have in the past and currently have initiated litigation to protect our intellectual property rights. Litigation may be necessary in the future to enforce our intellectual property rights (including patents), to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. Litigation could result in substantial costs and diversion of resources, and could also result in a decision that our intellectual property is invalid or unenforceable and, could adversely affect our business, future results of operations and financial condition. See the section headed “Business Overview—Intellectual Property.”

**We depend on third parties to manufacture, assemble and test our products and, if they are unable to do so, our ability to ship products and our business and results of operations will be harmed.**

We do not own or operate the integrated circuit fabrication facilities that manufacture the products we design. Three foundries, China Resources Microelectronic Limited (“CR Micro”), Vanguard International Semiconductor Corporation (“VIS”), and X-FAB Silicon Foundries SE (“X-FAB”), manufactured most of the integrated circuit products that we sold in 2016. These foundries manufacture integrated circuit products for us according to purchase orders. We do not have a guaranteed level of production capacity at any of these foundries, and any one or more could raise prices without notice. Although we provide the foundries with rolling forecasts of our production requirements, the ability of each foundry to provide wafers to us is limited by the foundry’s available capacity. The term “wafers” refers to slices of silicon used to manufacture integrated circuits, and it is one of the principal raw materials in our products. These foundries could choose to prioritize capacity for other customers, particularly larger customers, reduce or eliminate deliveries to us on short notice or increase the prices they charge us. Accordingly, we cannot be certain that these foundries will allocate sufficient capacity, if any, to satisfy our requirements particularly during any industry-wide capacity shortages. In addition, if any of these foundries were unable to continue manufacturing our products in the required volumes at acceptable quality, yields and costs or in a timely manner, our business and results of operations would be seriously harmed.

There are other significant risks associated with our reliance on these foundries, including the disruption in our ability to ship products caused by the length of time, which could be as much as 12 to 18 months. This disruption could require us to find alternative foundries for existing or new products; the reduction or elimination of deliveries to us by these outside foundries caused by a sudden increase in demand for semiconductor devices or a sudden reduction or elimination of manufacturing capacity by any existing manufacturers of semiconductor devices; the unavailability of, or delays in obtaining access to, key process technologies used by these foundries; and the susceptibility of our outside foundries to production interruptions resulting from natural disasters. Any of these events could cause these foundries to reduce or eliminate deliveries to us and cause disruption in our ability to ship products to our customers, which could negatively affect our business and results of operations.

We also rely on independent subcontractors to assemble and test most of our integrated circuit products. We do not have long-term agreements with some of these subcontractors but obtain services from them primarily on a purchase order basis. Our reliance on these subcontractors involves risks such as reduced control over delivery schedules, quality assurance and costs. These risks could result in product shortages or increase our costs of manufacturing, assembling or testing our products. If these subcontractors were unable or unwilling to continue to provide assembly and test services and deliver products at acceptable quality, yields and costs or in a timely manner, our business would be seriously harmed. We would also have to identify and qualify substitute subcontractors, which would be time consuming and costly and could result in unforeseen operational difficulties.

**If we cannot compete effectively against new and existing competitors, our net sales and gross margins could be harmed.**

Our ability to compete successfully in the market for integrated circuit products depends on factors both within and outside our control, including, but not limited to, any one or a combination of the following: i) our success in designing and subcontracting the manufacture of new products that implement new technologies and satisfy our customers' needs; ii) the performance of our products across a variety of parameters, such as reliability and cost efficiency; iii) the price of our products and those of our competitors; iv) our ability to control production costs; and v) the features of our competitors' products.

We believe our principal competitors include Intersil Corporation, Linear Technology Corporation, Maxim Integrated Products, Inc., Monolithic Power Systems, Inc., Ricoh Company, Ltd., Richtek Technology Corporation, Rohm Co., Ltd, Silergy Corporation and Texas Instruments Incorporated. There is also competition from the internal integrated circuit design and manufacturing capabilities of some of our existing and potential customers, such as Panasonic and Samsung. In addition to these competitors, other integrated circuit companies may decide to enter the market with analog and mixed-signal integrated circuit products that compete with our products or incorporate functions similar to those provided by our products.

Some of our competitors, such as Texas Instruments, have greater name recognition, their own manufacturing capabilities, significantly greater financial and technical resources, and the sales, marketing and distribution strengths that are normally associated with large multinational companies. These competitors may also have pre-existing relationships with our customers or potential customers. These competitors may be able to introduce new technologies more quickly, address customer requirements more rapidly, and devote greater resources to the promotion and sale of their products that are beyond our capability. Further, in the event of a manufacturing capacity shortage, these competitors may be able to manufacture products themselves or obtain third-party manufacturing capability when we are unable to do so.

**We have substantial operations outside of the United States that expose us to risks specific to our international operations that could harm our net sales and net income.**

As of December 31, 2016, a substantial portion of our operations, most of our employees, and most of the third parties we use to manufacture, assemble and test our products were located in China and Taiwan. In addition, sales outside the United States as a percentage of net sales accounted for almost all of our sales in the years ended December 31, 2016, 2015, 2014, 2013, and 2012. We expect our non-U.S. operations to grow and non-U.S. sales to continue to account for a substantial percentage of our net sales.

We are subject to risks specific to our international business operations, including: the risk of supply disruption, production disruption or other disruption arising from natural disasters; the outbreak of any severe communicable disease or other widespread health problems; the risk of potential conflict and political instability in the relationship between Taiwan and China, China and Japan, or North and South Korea; risks related to international political instability; risks associated with the European financial crises, the political uncertainty in Eastern European and their effects on the global financial markets; unpredictable consequences on the economic conditions in the U.S. and the rest of the world arising from terrorist attacks and other military or security operations; unexpected changes in regulatory requirements or legal uncertainties regarding tax regimes, that could result in tariffs and other trade barriers (including current and future import and export restrictions); difficulties in staffing and managing international operations; adverse effects of changes in foreign currency exchange rates on our results of operations; limited ability to enforce agreements, intellectual property and other rights in foreign countries; changes in labor conditions and requirements; longer payment cycles and greater difficulty in collecting accounts receivables; burdens and costs of compliance with a variety of foreign laws; expropriation of private enterprises; and reversal of the current policies (including favorable tax and lending policies) encouraging foreign investment or foreign trade by our host countries. In addition, the geographical distances between Asia, the U.S., the Cayman Islands and Europe also create a number of logistical and communication challenges. Although we have not experienced any serious harm in connection with our international operations, we cannot assure you that such problems will not arise in the future.

In addition, our reporting currency is the U.S. dollar, but our functional currency is the local currency of the respective entities. Therefore, a significant portion of our operating expenses is denominated in currencies other than the U.S. dollar, primarily the Renminbi and the New Taiwan dollar. As a result, appreciation or depreciation of other currencies in relation to the U.S. dollar could result in material transaction or translation gains or losses that could adversely affect, or cause fluctuations in, our results of operations. We do not currently engage in currency hedging activities.

**If we cannot adapt our product offerings to respond to rapid technological changes, our net sales will be harmed.**

The markets for consumer electronics, computer, industrial, communications, and automotive products, and the components used in these products, are characterized by rapidly changing technology and very frequent new product introductions by our direct customers and our competitors. For example, the microprocessor, display and battery technologies with which our products inter-operate change very rapidly. Although our products integrate analog and mixed-signal circuits and therefore may have substantially longer life-cycles than digital integrated circuits, we must still update our products or introduce new ones on a regular basis. If we do not respond in a timely manner to technological changes and new product introductions by our direct customers and competitors, we will be unable to maintain and grow our product sales. In addition, the emergence of significantly more efficient or cost-effective microprocessor, display and battery technologies could lessen the need for the power management functionality of our products, which would harm our net sales.

**Any impairment charges may have a material adverse effect on our net income.**

In accordance with accounting principles generally accepted in the United States, we are required to evaluate our investments, long-lived assets and intangible assets for impairment whenever triggering events or changes in circumstances indicate that the asset may be impaired. If certain criteria are met, we are required to record an impairment charge. For example, we hold cost method securities and long-lived assets, some of which have incurred certain impairment charges as discussed further in our financial statements. We currently are not able to estimate the extent or timing of any impairment charge for future years. Any impairment charge required may have a material adverse effect on our net income. The determination of an impairment charge at any given time is based significantly on our expected results of operations over a number of years subsequent to that time. As a result, an impairment charge is more likely to occur during a period when our operating results are otherwise already depressed. See "Item 5. Operating and Financial Review and Prospects — Critical Accounting Policies" for a discussion of how we assess if an impairment charge is required and, if so, how the amount is determined.

**We will need to recruit and retain qualified personnel to grow our business successfully.**

Our future success will depend on our ability to attract and retain experienced sales, research and development, marketing, customer support and management personnel. If we do not attract and retain these personnel, our ability to grow our business, sell our products, enter new markets and increase our share of existing markets could be harmed. There can be no assurance that we will be successful in hiring for these positions in the near future. Our sales strategy requires that we hire additional direct sales persons and independent sales representatives in our major markets. Moreover, our independent sales representatives and direct sales personnel must market our products effectively and be qualified to provide timely and cost-effective customer support and service. If they are unable to do so, or if we are unable to expand these organizations, this could harm our ability to increase our net sales and limit our ability to sell our products and/or expand our market share. Competition for qualified personnel in digital, analog and mixed-signal integrated circuit design is intense. In the past, we have experienced difficulty in recruiting and retaining qualified personnel, especially technical and sales personnel. As we intend to expand the scope of our international operations, this will require us to attract experienced management, research and development, marketing, sales and customer support personnel for our international offices. We expect competition for qualified personnel to remain intense, and we may not succeed in attracting or retaining such personnel. In addition, new employees generally require substantial training in our design methodology, design flow and technology, which in turn requires significant resources and management attention. There is a risk that even if we invest significant resources in attempting to attract, train and retain qualified personnel, we will not be successful in our efforts. In that event, our costs of doing business would increase without a corresponding increase in net sales.

Our success will depend to a significant extent on the continued service of our executive officers, including Sterling Du, our chief executive officer and chairman of our board, and other key employees, including key sales, consulting, technical, marketing and legal personnel. If we lose the services of one or more of our executives or key employees, our business and ability to implement our business objectives successfully could be harmed, particularly if one or more of our executives or key employees decide to join a competitor or otherwise compete directly or indirectly with us.

**Defects in our products could result in significant costs and could impair our ability to sell our products.**

Detection of any significant defects in our products may result in, among other things, loss of or delay in market acceptance and sales of our products, diversion of development resources, injury to our reputation and increased service and warranty costs. Because our products are complex, they may contain defects that can be present at any point in a product's life cycle. These defects could harm our reputation, which could result in significant costs to us and could impair our ability to sell our products. The costs we may incur in correcting any product defects may be substantial and could materially adversely affect our results of operations. While we continually test our products for defects and work with customers through our customer support services to identify and correct problems, defects in our products may be found in the future. Testing for defects is complicated in part because it is difficult to simulate the highly complex environments in which our customers may use our products. In the past, when we have discovered defects in our products, we also experienced delays in the shipment of our products. These delays have principally related to new product update releases. To date, none of these delays has materially affected our business; however, product defects or delays in the future could be material, and adversely affect our reputation and our ability to sell our products.

**A substantial portion of our net sales is generated by a small number of customers. If any of these customers delays or reduces its orders, our net sales and earnings may be harmed.**

Historically, a relatively small number of customers has accounted for a significant portion of our net sales in any particular period. We have no long-term volume purchase commitments from any of our significant customers. We cannot be certain that our current customers will continue to place orders with us and/or at the levels of previous periods, in addition to obtaining orders from new customers. In addition, some of our customers, acting as intermediary manufacturers, supply products to end-market purchasers, and any of these end-market purchasers could choose to reduce or eliminate orders for our customers' products. This would in turn lower our customers' orders for our products.

For the year ended December 31, 2016, one customer accounted for 10% of our net sales. For the year ended December 31, 2015, one customer accounted for 11% of our net sales. For the year ended December 31, 2014, two customers accounted for 12% and 10% of our net sales. The changes in sales to these customers as a percentage of our total net sales have been caused by a number of factors, including, without limitation, the reduction, delay or cancellation of orders from one or more of our significant customers, some of which were outside our control. We anticipate that sales of our products to a relatively small number of customers will continue to account for a significant portion of our net sales.

**Our ability to manage growth will affect our ability to achieve and maintain profitability.**

Our ability to achieve and maintain profitability will depend in part on our ability to implement and expand operational, customer support and financial control systems and to train and manage our employees. We may not be able to augment or improve existing systems and controls or implement new systems and controls in response to future growth, if any. In addition, we will need to expand our facilities to accommodate the growth in our personnel. Any failure to manage growth could divert our attention from successfully executing our business plan and adversely affect our ability to expand our business successfully. Our historical growth has placed, and any further growth is likely to continue to place, a significant strain on our resources. In order to grow successfully, we will need to maintain close coordination among our executive, engineering, accounting, finance, legal, marketing, sales, operations and customer support organizations, particularly in light of the internationally dispersed nature of our operations.

**Third parties have asserted, and in the future could assert, that our products infringe their intellectual property rights. These claims could harm our ability to sell our products and expose us to litigation.**

As is typical in the semiconductor industry, we have periodically received communications from third parties asserting patents that cover certain of our technologies or products, and alleging infringement of certain of their intellectual property rights. We may receive similar communications in the future. In the event any third party were to make a valid claim against us or our customers, we could be enjoined from selling selected products such (including our lighting or power products), or we could be required to pay royalties to third parties, which would increase the cost of our products. Third-party infringement claims, with or without merit, have been, and could potentially be, time consuming, result in substantial diversion of our resources, incur significant litigation costs (including costs related to any fines and/or damages we may owe), cause product shipment delays, prevent us and/or our customers from selling some or all of our products, cause our customers or end-users not to use our products, or require us to enter into license agreements that could adversely affect our cost structure (and, in turn, our competitiveness), which may not be available on acceptable terms, or at all. Any such event could seriously harm our business and our results of operations. We expect that semiconductor companies will increasingly be subject to infringement claims as the number of products, non-practicing patent entities and competitors in the semiconductor industry grows. See the section headed "Business Overview—Intellectual Property."

From time to time, in the normal course of business, we agree to indemnify third parties with whom we enter into contractual relationships, including customers and parties to other transactions with us, with respect to certain matters. We have agreed, under certain conditions, to hold these third parties harmless against specified losses, such as those arising from a breach of representations or covenants, other third-party claims that our products when used for their intended purposes infringe the intellectual property rights of such other third parties or other claims made against certain parties. It is not possible to determine the maximum potential amount of liability under these indemnification obligations due to our limited history of prior indemnification claims and the unique facts and circumstances that are likely to be involved in each particular claim. To date, we have not made any payments under these obligations.

Until all outstanding litigation matters are completely resolved, we will continue to incur substantial legal expenses that vary with the level of activity in each legal proceeding. This level of activity is not entirely within our control, especially if we need to respond to legal actions directly or on behalf of our customers. Consequently, we may find it difficult to predict the legal expenses for any given period, which will impair our ability to forecast our results of operations for that period. For example, the level of legal expenses is not entirely within our control as we may need to respond to legal actions by opposing parties or scheduling decisions by the judges which could occur with relatively short notice. It is difficult for us to forecast our legal expenses for any given quarter, which adversely affects our ability to forecast our expected results of operations in general.

Given the inherent uncertainties in litigation, there cannot be any assurance that we will prevail in any particular litigation matter, nor can we predict the outcome of any such litigation. If any party were to prevail in its claims against us, our rights to certain patents and results of operations could be materially adversely affected. In any litigation arising from claims that we infringe on the intellectual property rights of others, an adverse result could involve an injunction that could prevent the sales of a material portion of our products, and a reduction or the elimination of the value of related inventories, any of which could have a material adverse effect on our net sales, results of operations and financial condition. See the section headed "Business Overview—Intellectual Property."

**We may be subject to lawsuits from third parties, which could harm our earnings and expose us to additional uncertainties.**

We are a defendant or plaintiff in actions that arise in the normal course of business as well as actions that arose as counterclaims in response to our patent infringement actions, including actions for antitrust, unfair competition and interference. We do not believe that the amount of ultimate liability of other unresolved proceedings will materially affect our financial position, overall trends in results of operations, or liquidity. However, the ultimate outcome of any litigation or claim is uncertain, and the impact of an unfavorable outcome could be material to us.

**Changes in local laws, rules and regulations could have an adverse effect on our ability to protect our intellectual property or other aspects of our business.**

Our business activities and intellectual property is dependent on various regulations in countries where we operate, including, but not limited to, business and investment approval, export regulations, tariffs, accounting standards and taxation. We must also adhere to various laws and regulations concerning trading, antitrust practices, product liability, consumer protection, intellectual property rights, product safety, the environment and recycling, and internal control. Changes in such laws and regulations, and additional expenses to comply with any such amendments, may affect our business results and financial position. Further, changes in intellectual property laws could negatively affect our ability to protect our patents and other intellectual property in one or several jurisdictions.

**If we fail to maintain an effective system of internal controls, we may not be able to report our financial results adequately. As a result, we may fail to meet our reporting obligations and current and potential holders of ADSs and/or ordinary shares could lose confidence in our financial reporting, which could adversely affect the trading price of our ADSs.**

Effective internal controls are necessary for us to provide reliable financial reports. If we cannot provide reliable financial reports or prevent fraud, our results of operations could be misstated, our reputation may be harmed and the trading price of our ADSs could be adversely affected. We cannot be certain that our controls over our financial processes and reporting will continue to be adequate in the future. Any failure of our internal controls over financial reporting could result in a material misstatement in financial statements.

In addition, under Section 404 of the Sarbanes-Oxley Act, we are required to furnish a report by our management on our internal control over financial reporting. This report contains, among other matters, an assessment of the effectiveness of our internal control over financial reporting as of the end of our fiscal year, including a statement as to whether or not our internal control over financial reporting is effective. This assessment must include disclosure of any material weaknesses in our internal control over financial reporting identified by management.

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, 2016. 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 Independent 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, and could result in lawsuits being filed against us by our stockholders or otherwise harm our reputation.

**Our transfer pricing procedures may be challenged by tax or regulatory authorities or "taxing authorities", which may subject us to higher taxes and adversely affect our earnings.**

Transfer pricing refers to the prices that one member of a group of affiliated corporation charges to another member of the group for goods, services or the use of intellectual property. If two or more affiliated corporations are located in different countries, the laws or regulations of each country generally will require that transfer prices be the same as those charged by unrelated corporations dealing with each other at arm's length. If one or more of the countries in which our affiliated corporations are located believe that transfer prices were manipulated by our affiliated corporations in a way that distorts the true taxable income of the corporations, the laws of such countries could require us to redetermine transfer prices and thereby reallocate the income of our affiliate corporations in order to reflect such income clearly. Any reallocation of income from one of our corporations in a lower tax jurisdiction to an affiliated corporation in a higher tax jurisdiction would result in a higher overall tax liability to us. Moreover, if the country from which the income is being reallocated does not agree to the reallocation, the same income could be subject to taxation by both countries.

We have adopted transfer pricing agreements with our subsidiaries located in the United States, China, and Taiwan to regulate inter-company transfers. A transfer pricing agreement is a contract for the transfer of goods, services or intellectual property from one corporation to a related corporation that sets forth the prices that the related parties believe are those charged by unrelated corporations dealing with each other at arm's length. In this regard, we are subject to risks not faced by other companies with international operations that do not create inter-company transfers. If the taxing authorities of any jurisdiction, including Taiwan, China, and the United States, were to challenge these agreements successfully or require changes in our transfer pricing practices, we could become subject to higher taxes and our earnings would be adversely affected. There can be no assurance that we will continue to be found to be operating in compliance with transfer pricing laws, or that such laws will not be modified, which, as a result, may require changes to our transfer pricing practices or operating procedures. Any determination of income reallocation or modification of transfer pricing laws could result in an income tax assessment of the portion of income deemed to be derived from the taxing jurisdiction that so reallocates the income or modifies its transfer pricing laws.

**Sales of our products could decline if our products fail to support evolving industry standards or environmental requirements.**

Our net sales are mainly derived from sales of integrated circuit products that are components of electronic devices built to industry standards, individual country specifications and other widely accepted specifications. Our products must be designed to conform to these standards and specifications in order to achieve market acceptance. Technology standards and specifications continually evolve, and we may not be able to successfully design and manufacture new products that conform to these new standards or specifications in a timely manner. Additionally, new products we develop to conform to new specifications in some markets may not be accepted in other markets.

**Climate change, use of Conflict Minerals, other environmental concerns and green initiatives also presents other commercial challenges, economic risks and physical risks that could harm our results of operations or affect the manner in which we conduct our business.**

Increasing climate change and environmental concerns could affect the results of our operations if any of our customers would request us to exceed any standard(s) set for environmentally compliant products and services. For example, we have been working with our suppliers, customers, and several industry consortia to develop and provide EU "RoHS" (European Union Restriction of Hazardous Substances) compliant products. We have also implemented procedures to comply with the requirements of the Securities Exchange Act to comply with Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") regarding the reporting of Conflict Minerals in use, as defined by the Dodd-Frank Act. If we or our suppliers, vendors and manufacturers are able to offer such products or offer products that are compliant with these standards, but said products are not as reliable due to the lack of reasonably available alternative technologies or materials, we may lose market share to our competitors. Furthermore, while we have implemented procedures to comply with these requirements, our suppliers, vendors and/or manufacturers could fall out of compliance with said requirements without our knowledge.

**Provisions in our Memorandum and Articles of Association may discourage potential acquisition bids for us and prevent changes in our management that our shareholders may favor.**

Provisions in our Memorandum and Articles of Association could discourage potential acquisition proposals and could delay or prevent a change in control transaction that our shareholders favor. These provisions could have the effect of discouraging others from making offers for our ordinary shares or ADSs. As a result, these provisions may prevent the trading price of our ADSs from reflecting the effects of actual or rumored takeover attempts and may prevent shareholders from reselling their ordinary shares or ADSs at or above the price at which they purchased their ordinary shares or ADSs. These provisions may also prevent changes in our management that our shareholders may favor. Our Memorandum and Articles do not permit shareholders to act by written consent, do not permit shareholders to call a general meeting and provide for a classified board of directors, which means shareholders can only elect a limited number of our directors in any given year. Furthermore, our board has the authority to issue up to 250,000,000 preference shares in one or more series. Our board can fix the price, rights, preferences, privileges and restrictions of such preference shares without any further vote or action by our shareholders but subject to any direction that may be given by the shareholders in a general meeting. The issuance of preference shares may delay or prevent a change in control transaction without further action by our shareholders or make removal of management more difficult.

**As we are a Cayman Islands company, it could be difficult for investors to effect service of process on and recover against us or our directors and officers and our shareholders may face difficulties in protecting their interest.**

We are a Cayman Islands company, and many of our officers and directors are residents of various jurisdictions outside the United States. A substantial portion of our assets and the assets of our officers and directors, at any one time, are and may be located in jurisdictions outside the United States. Although we have irrevocably agreed that we may be served with process in Santa Clara, California with respect to actions arising out of or in connection with United States federal securities laws relating to offers and sales of our ordinary shares and/or our ADSs, it could be difficult for investors to effect service of process within the United States on our directors and officers who reside outside the United States, or to recover against us or our directors and officers on judgments of the United States courts predicated upon the civil liability provisions of the United States federal securities laws.

Our corporate affairs are governed by our charter documents, consisting of our Memorandum and Articles of Association, and by the Companies Law and common law of the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors are governed by Cayman Islands law, which are not as clearly established as under statutes or judicial precedent in jurisdictions such as the United States. While there is some case law in the Cayman Islands on these matters, it is not as developed as, for example, in the United States. In addition, the laws of the Cayman Islands relating to the protection of the interests of minority shareholders differ in some respects from those established under statutes or judicial precedent in existence in the United States. Such differences may mean that our minority shareholders may have less protection than they would have under the laws of the United States. Due to the less protective nature of such laws in the Cayman Islands, our shareholders may have more difficulty in protecting their interests in the face of actions by our management or directors than would shareholders of a corporation incorporated in some other jurisdictions.

**We may become a passive foreign investment company, which could result in adverse U.S. tax consequences to U.S. investors.**

We may be classified as a passive foreign investment company by the U.S. Internal Revenue Service for U.S. federal income tax purposes. Such characterization could result in adverse U.S. tax consequences to you if you are a U.S. investor. For example, if we are a passive foreign investment company, our U.S. investors will become subject to increased tax liabilities under U.S. tax laws and regulations and will become subject to burdensome reporting requirements. The determination of whether or not we are a passive foreign investment company is made on an annual basis and depends on the composition of our income and assets, including goodwill, from time to time. Specifically, we will be classified as a passive foreign investment company for U.S. tax purposes if, after the application of look-through rules, either (a) 75% or more of our gross income in a taxable year is passive income, or (b) the average percentage of our assets (by value) in a taxable year that produce or are held for production of passive income is at least 50%. Our judgment is not binding on the Internal Revenue Service. We cannot assure you that we will not be a passive foreign investment company for the current or any future taxable year. See “Taxation—United States Federal Income Taxation—Passive Foreign Investment Company.”

**Holders of ADSs may not be able to exercise their right to vote.**

Holders of our ADSs may instruct the depository of our ADSs to vote the ordinary shares underlying their ADSs but only if we ask the depository to ask for instructions. Otherwise, they will not be able to exercise their right to vote unless they withdraw the ordinary shares underlying the ADSs they hold. However, they may not know about the meeting sufficiently enough in advance to withdraw those ordinary shares. If we ask for instructions, the depository will notify the holders of the upcoming vote and arrange to deliver our voting materials to them. We cannot assure you that holders will receive the voting materials in time to ensure that they can instruct the depository to vote their ordinary shares. In addition, the depository and its agents are not responsible for failing to carry out voting instructions or for the manner of carrying out voting instructions. This means that holders may not be able to exercise their right to vote, and there is no guarantee that the ordinary shares underlying your ADSs would be voted as requested.

**The depository for our ADSs may give us a discretionary proxy to vote the ordinary shares underlying your ADSs if holders of ADSs do not vote at shareholders’ meetings which could adversely affect their interests.**

Under the deposit agreement for the ADSs, the depository will give us a discretionary proxy to vote the ordinary shares on behalf of the underlying ADSs at shareholders’ meetings if the holder of the ADSs did not vote, unless we notify the depository that we do not wish to receive said discretionary proxy. Examples where we would not want to receive or exercise a discretionary proxy include, without limitation, instances where we think there is substantial shareholder opposition to the particular question, or we think the particular question would have a material adverse impact on our shareholders.

The effect of this discretionary proxy is that holders of ADSs cannot prevent the ordinary shares underlying their ADSs from being voted, absent the situation described above, and it may make it more difficult for shareholders to influence the management of our company. Holders of our ordinary shares are not subject to a discretionary proxy.

**Holders of ADSs may not receive distributions on ordinary shares or any value for them if it is illegal or impractical to make them available.**

The depository of our ADSs has agreed to pay to ADS holders the cash dividends or other distributions it or the custodian for our ADSs receives on ordinary shares or other deposited securities after deducting its fees and expenses. Holders of our ADSs will receive these distributions in proportion to the number of ordinary shares the ADSs represent. However, the depository is not responsible if it decides that it is unlawful or impractical to make a distribution available to any holders of ADSs. We have no obligation to take any other action to permit the distribution of our ADSs, ordinary shares, rights or anything else to holders of our ADSs. This means that ADS holders may not receive the distributions we make on ordinary shares or any value for them if it is illegal or impractical for us to make them available. These restrictions may have a material adverse effect on the value of the ADSs.



#### **Holders of ADSs may be subject to limitations on transfer of ADSs.**

ADSs represented by American Depositary Receipts (“ADRs”) are transferable on the books of the depository. However, the depository may close its books at any time or from time to time when it deems expedient in connection with the performance of its duties. The depository may refuse to deliver, transfer or register transfers of our ADSs generally when our books or the books of the depository are closed, or at any time if we or the depository thinks it is advisable to do so because of any requirement of law or any government or governmental body, or under any provision of the deposit agreement, or for any other reason.

#### **ITEM 4. INFORMATION ON THE COMPANY**

##### **HISTORY AND DEVELOPMENT OF THE COMPANY**

Our legal name is O<sub>2</sub>Micro International Limited. We are incorporated in the Cayman Islands. Our registered office is located at Maples Corporate Services Limited, Uglund House, P.O. Box 309, South Church Street, Grand Cayman KY1-1104, Cayman Islands. Our principal executive offices are located at Grand Pavilion Commercial Centre, West Bay Road, P.O. Box 32331 Grand Cayman KY1-1209, Cayman Islands. Our telephone number is (345) 945-1110. We have a subsidiary, O<sub>2</sub>Micro, Inc., which was incorporated as a California corporation in March 1995. In March 1997, O<sub>2</sub>Micro International Limited was incorporated as a Cayman Islands company. In March 1997, we exchanged our ordinary shares and preference shares for common stock and preferred stock of O<sub>2</sub>Micro, Inc. After the exchange, we held all of the outstanding capital stock of O<sub>2</sub> Micro, Inc., our wholly owned subsidiary in the United States. Our shares were initially listed on NASDAQ on August 23, 2000 and on the Cayman Islands Stock Exchange on February 1, 2001. On November 25, 2005, we effected a 50-for-1 share split of our ordinary shares and created an ADS program for our ADSs to be quoted on NASDAQ, with each ADS representing 50 ordinary shares. We delisted our ordinary shares from NASDAQ on November 25, 2005 and listed our ADSs on NASDAQ on November 28, 2005, the next trading day. We subsequently listed our ordinary shares on the SEHK in Hong Kong on March 2, 2006, by way of introduction. On February 27, 2009, we submitted an application for the voluntary withdrawal of the listing of ordinary shares (“Shares”) on the Main Board of the SEHK (collectively referred to as the “Proposed Withdrawal”) for reasons of cost and utility. We have retained our existing primary listing of ADSs on NASDAQ following the Proposed Withdrawal and for the foreseeable future. The Proposed Withdrawal was approved at the Extraordinary General Meeting of Shareholders held on May 30, 2009, and the listing of the Shares on the SEHK was withdrawn on September 9, 2009.

Our agent for service of process in the U.S. for the purpose of our securities filings is our chief executive officer, Sterling Du, c/o O<sub>2</sub>Micro, Inc., 3118 Patrick Henry Drive, Santa Clara, CA 95054.

We have incorporated various wholly-owned subsidiaries, including (among others) O<sub>2</sub>Micro Electronics, Inc. (“O<sub>2</sub>Micro-Taiwan”), O<sub>2</sub>Micro International Japan Ltd. (“O<sub>2</sub>Micro-Japan”), and O<sub>2</sub>Micro (China) Co., Ltd. (“O<sub>2</sub>Micro-China”). O<sub>2</sub>Micro-Taiwan is engaged in operations and sales support services. O<sub>2</sub>Micro-Japan is engaged in sales support services. O<sub>2</sub>Micro-China and other subsidiaries are mostly engaged in research and development services.

For the three years ended December 31, 2016, our principal capital expenditures were approximately \$2.4 million in the purchase of property and equipment.

##### **BUSINESS OVERVIEW**

Our business focuses on designing, developing and marketing high performance integrated circuits and solutions for manufacturers of products in the consumer electronics, computer, industrial, communications, and automotive markets. We have targeted, and are designing products for, applications such as LCD and LED monitors, LCD and LED televisions, notebook computers, tablet computers, low/zero emission vehicles, mobile phones, power tools, energy efficient technology relating to sophisticated batteries, LED lighting including general lighting, and portable electronics devices. Some of the features of our integrated circuit products include the following: managing and providing power for LCD and LED lighting; controlling and monitoring battery charging and discharging in portable electronic devices and vehicles; performing DC/DC and AC/DC conversion; and providing select and switch functionality between power sources.

We believe that our focus on these products provides us with an opportunity to participate in large and growing markets. Potential future growth in the LED television, mobile computing, communications, electric vehicles, power tools, uninterrupted power supplies and general lighting represents attractive growth opportunities.

Our integrated circuit products use analog and mixed-signal designs that combine analog and digital circuits on a single chip, reducing the number of components needed for function performance, thereby allowing our customers to reduce the size, weight, power requirements and/or cost of their products. We offer a wide range of proprietary application specific standard products as well as customized products. We work closely with our customers to identify their product needs and establish engineering priorities for new product designs and development. We believe that our system-level expertise and extensive experience with power management systems allow us to more effectively develop proprietary solutions and foster long-term relationships with our customers.

We sell our products to OEMs, ODMs and module makers. Our integrated circuits have been incorporated into products sold by Acer, Dell, General Electric, Hewlett-Packard, Lenovo, LG Electronics, NEC, Panasonic, Samsung Electronics, Sharp, Skyworth, Sony, TCL, and Toshiba, among others. We sell our products through our direct sales force, independent sales representatives and/or distributors in Asia and North America. We also have design centers in many of our key markets to provide design and engineering support to our customers. We outsource the fabrication of our products to standard high volume semiconductor foundries. This “fabless” approach allows us to focus on product development, minimize fixed costs and capital expenditures, and access diverse manufacturing technologies.

## **Industry Background**

The markets for consumer electronics, mobile computing and communications products, such as LCD monitors, LCD and LED televisions, tablets, mobile handsets and portable entertainment devices, are large and growing as functionality increases and prices decrease. One of the most significant challenges in these markets remains the efficient management of power. As the number of applications and features available for these products has increased, the number and variety of power loads, or individual subsystems requiring voltage or current regulation, has also grown. Each additional application or feature can require multiple functions and circuits that, in turn, require more individually-regulated and managed power sources. Increasingly, manufacturers are turning to innovative new semiconductor technologies to manage the available power source capacity more efficiently.

Power management integrated circuits deliver power and regulate voltage, controlling the flow of electrical energy among the various power loads and energy sources in a product or system. Power management requires a combination of two distinct technological disciplines: digital integrated circuit design and analog integrated circuit design. Digital circuits, such as microprocessor and memory semiconductors, provide most of the functionality of computer processing. However, digital circuits generally cannot handle significant amounts of current or multiple voltage levels. In contrast, analog circuits use and manipulate continuously varying voltage and current levels. Battery power systems, which have relatively high and continuously varying power levels, are inherently analog systems.

Digital integrated circuit technology can be used to manage power systems more intelligently and efficiently and help to prolong battery life in mobile applications. However, since battery power systems are analog by nature, mixed-signal integrated circuits, or circuits that incorporate both digital and analog technologies, are necessary in order to harness the intelligence provided by digital technology. Designing mixed-signal integrated circuits poses a number of difficulties: analog circuits are more sensitive than digital circuits to the physical layout and electrical characteristics of the circuit; analog circuit designers must have a very high level of circuit design experience; and basic differences in the technologies used in digital and analog circuit design make combining the technologies problematic.

In addition, mixed-signal integrated circuits comprise both digital and analog components, and the trend toward more complex devices has increased the number of components substantially. Integrating the functions of those components on a single chip, known as a system-on-a-chip, can enable manufacturers to make products smaller, lighter, and more reliable. Thus, as mobile computing and communications devices grow in complexity and functionality, there is an increasing need for higher levels of systems integration. In addition, variances in battery designs among manufacturers make it more difficult to design intelligent systems that are optimized for particular power systems.

Most consumer electronics, mobile computing and communications product manufacturers need mixed-signal and analog integrated circuits specifically designed to optimize the power system usage in their devices to enable them to offer new devices with richer functionality and longer battery lives. These semiconductors should also be highly integrated and standards-based to help manufacturers create products that are smaller, lighter, easier to use, more reliable and more cost-efficient to design and produce. In addition, in mobile device markets where product life cycles can be less than one year, these solutions typically need to be developed using advanced design methodologies to allow manufacturers to achieve rapid time-to-market with their new products.

Several different process technologies are available for designing and fabricating analog and digital integrated circuits. Of these, complementary metal oxide semiconductor, or CMOS, is the most widely used process technology, especially for purely digital integrated circuits. CMOS processes are described in terms of feature size, or geometry, and are measured in microns. One micron equals one millionth of a meter. Currently, advanced process technologies achieve feature sizes of 0.09 micron, 0.065 micron, 0.04 micron and smaller. However, small feature size circuits can become damaged when exposed to high voltages and therefore power management integrated circuits are typically fabricated using larger feature sizes. For this reason, older manufacturing facilities, or fabs, having feature sizes of 0.18 micron and 0.5 micron or greater, have traditionally been used in fabricating power management integrated circuits, while the most advanced, and most expensive fabs are used for digital and non-power management analog integrated circuits.

## **Products**

We market power management components and solutions for the communications, computer, consumer, industrial, and automotive markets. Our power management products include ICs to i) provide power for LCD and LED lighting, ii) control and monitoring of battery charging and discharging, iii) DC/DC and AC/DC conversion, iv) provide select and switch functionality between power sources. In particular, our core technologies in the Application Specific Integrated Circuit (“ASIC”) chips are our exclusive, proprietary technology, which allows us to deliver enhanced performance and service to our customers. The majority of our products are sold into the following five end-markets:

- **Consumer electronics market**, including LCD and LED televisions, desktop and notebook monitors, portable media players, digital cameras, GPS/PND solutions for directional assistance, PDAs, games, and general lighting products (including LED light bulbs);
- **Computer market**, including desktop computers, LCD and LED monitors, tablet computers, notebooks, netbooks, and mobile communication applications;
- **Industrial market**, including any product that is specified to operate over an extended temperature range, i.e., beyond the standard commercial operating temperature range of standard semiconductor products (zero degrees to 70 degrees centigrade). These products include battery management systems for power tools, electric bikes, LEV applications, LCD and LED monitors, notebooks, netbooks, industrial PCs, and general lighting products;
- **Communications market**, including portable media devices, Smart Phones, PDAs, and other portable electronic applications; and
- **Automotive market**, including GPS units for navigational assistance in vehicles, Electric and Hybrid Vehicle (EV/HEV) battery management, and in-vehicle passenger entertainment and communication systems.

The majority of our revenue is derived from the sale of our products in the consumer, industrial, and computer markets. Additionally, we have increased our efforts to expand our product portfolio addressing opportunities in the automotive and communications markets.

### **Marketing, Sales, and Customer Support**

Our marketing strategy is focused on the sale of proprietary analog and mixed-signal integrated circuits to customers in the consumer electronics, computer, industrial, communications, and automotive markets. These markets tend to be dominated by a small number of major brand name companies. As a result, we focus our resources on the major vendors in each market.

We primarily sell proprietary application specific products to our customers and work with them on new product development. We also design customized products for our customers. We work directly with our customers to create demand for our products by providing them with application specific product information for their system design, engineering and procurement groups. We actively participate in their design processes to introduce them to our products and the target applications our products address. We endeavor to design products that will meet increasingly complex and specific design requirements, but which will also support widespread demand for these future products. We typically undertake a four-to-eight month development process with our customers. If successful, this process culminates in a customer deciding to use our product in its system and/or products, which we refer to as a design win. Volume production generally takes an additional three-to-six months after the initial design win confirmation. Once our products are accepted and designed into an application, the customer is likely to continue to use the same power architecture and derivative products in a number of its models, which tends to extend our product life cycles.

We sell our products to OEMs, ODMs and module makers. We market and sell these products through a combination of our direct sales force, independent sales representatives and distributors. We maintain direct sales offices in most of our major markets which include China, Taiwan, Korea, and Japan.

We pay our direct sales force on a salary and performance bonus basis only. Our independent sales representatives are paid on a commission basis, based on a percentage of the actual sales referred by them. For sales through sales representatives, we invoice and deliver our products directly to the customers. We have also entered into distributorship arrangements with distributors for the sale of our products at the request of several of our major end-customers. For our other customers, sales are made through our direct sales offices in Japan, Taiwan, Korea and China. It is customary practice for OEMs, ODMs and module makers to purchase products like ours through distributors because of the ancillary services provided by them such as inventory storage, payment terms and conditions and just-in-time delivery. We may provide a discount on the prices of the products we sell to our distributors (as compared to the prices we offer to end customers), depending on the terms and conditions of the individual purchases. In certain limited cases, we sell products through distributors. We defer recognition of such sales until the product is sold by the distributors to its end customers. Products held by these distributors are considered part of our inventory and included in our inventory balance. We receive regular inventory reports from the distributors, which we use as part of our overall inventory control. We evaluate our inventory on a quarterly basis and full provision is made for inventory which is over six months old and without end customer demand based on forecasted product demand and market conditions.

Our marketing efforts include market analysis, participation in industry trade shows and technical conferences, sales training, publication of technical articles, maintenance of our web site and advertising. We maintain customer support staff in the United States, Taiwan, China, Japan, and Korea for post order servicing and applications support.

### **Seasonality**

The consumer electronics and computer markets are characterized by seasonal volume increases primarily driven by increased consumer spending during the holiday season. We normally experience the higher sales volume to our customers in these markets, when such customers increase their inventories in anticipation of increased seasonal demand. Our customers in the industrial and communications markets are to a lesser extent subject to seasonal consumer demand. As a result, our sales volume to those customers has been largely consistent from quarter-to-quarter.

## Customers

We focus on the major OEMs (or brand owners) in the consumer electronics, computer, industrial and communications markets. Many of these major OEMs use third-party providers, such as ODMs, module makers or other intermediaries, to produce their products or portions of their products containing our components. Hence, the majority of our direct sales are to these third-party providers.

We have no long-term volume sales contracts with any of our major customers. The majority of our sales to customers are conducted on the basis of purchase orders, which set out the specific terms for a particular sale. We price our products primarily with reference to the prevailing market conditions, taking into consideration the complexity, technology and features of the product, the order size and the relationship with the customer.

The table below sets forth, for the periods indicated, the dollar amount of our net sales to unaffiliated customers by geographic region:

	Years Ended December 31		
	2016	2015	2014
	<i>(in thousands)</i>		
China	\$ 46,784	\$ 45,854	\$ 55,133
Taiwan	3,009	2,274	2,022
Japan	2,535	3,759	4,490
Korea	2,257	879	288
Singapore	1,539	1,398	1,341
Other	437	677	317
	<u>\$ 56,561</u>	<u>\$ 54,841</u>	<u>\$ 63,591</u>

We generally extend to our customers credit terms varying from 30 to 60 days. We may adjust our usual credit terms according to each customer's credit history as well as local market practice. Our customers generally pay us either by direct wire transfer or under letter of credit arrangement. To date, we have not experienced any material problems relating to customer payments or material write-offs of accounts receivable due to uncollectability.

## Manufacturing

We subcontract the manufacture of our products and most of the testing for our products to semiconductor foundries, assembly and testing service providers. This "fables" approach allows us to focus on product development, reduce fixed costs and capital expenditures, and access diverse manufacturing technologies.

We use established mainstream processes for the manufacture of our products. This approach reduces our technical risks and minimizes the risks related to production capacity constraints.

### *Wafer Manufacturing*

Wafer manufacturing is a capital intensive and complex operation which takes place at dedicated facilities of semiconductor foundries. After we have designed our integrated circuits, we place orders with a semiconductor foundry to fabricate wafers with our integrated circuits embedded in them. The semiconductor foundry purchases raw unprocessed wafers, or silicon substrates, and processes them according to mutually agreed manufacturing specifications to fabricate the wafers used in our products. Currently, the majority of our wafers are fabricated using 0.18 to 1.0 micron CMOS semiconductor processes. The wafer fabrication process generally takes 6 to 10 weeks. Fabricated wafers are then shipped by the semiconductor foundry, according to our instructions, to either an assembly service provider or to an electrical wafer sort service provider.

Our major semiconductor foundry providers are CR Micro, VIS, and X-FAB. We do not enter into long-term contracts with our semiconductor foundry providers. They manufacture our products on a purchase-order basis in accordance with our specifications and requirements. In general, the cost charged to us for the foundry services depends on the manufacturing process technologies, as well as order size and foundry capacity utilization.

### *Assembly and Testing*

The fabricated wafers may or may not require electrical wafer sort prior to assembly. The completed wafers are either sent to an assembly service provider for assembly or held at our warehouse facilities, or an "inventory hub," for assembly at a later date. An inventory hub is a provider of warehousing services. We often hold inventory of our semi-finished products in wafer form because it is at this manufacturing stage that most time has been invested, with much of the cost not yet incurred, and we then have the flexibility of choosing the type of packaging into which they are to be assembled. The wafer sort and assembly process generally takes three to six weeks.

Once our integrated circuits are assembled and packaged, they are ready for final electrical testing. We instruct the assembly service provider to send our packaged integrated circuits to a testing service provider for final testing or our warehouse facilities (or an inventory hub) for testing at a later date. The electrical testing process generally takes a few days. Once our products have been tested, they are ready for use by our customers.

Finished products may be sent to our customers or their designees such as third party service providers that manufacture their products or a portion of their products containing our integrated circuits. Our customers may request for our integrated circuits to be shipped in plastic tubes or trays, several to a tube or tray, or use a form of packaging called “tape and reel” that more readily provides for automated assembly of our integrated circuits into their products. If a customer orders “tape and reel” packaging, this is done either at a testing service provider or a “tape and reel” service provider prior to shipment of our products to the customer.

We utilize several assembly and testing service providers in Taiwan, China and other areas of Asia on a purchase order basis. They assemble and test our products based on our specifications and requirements. In general, the cost charged to us for these assembly and testing services depends on prevailing market rates for these services and our relationship with the service provider. Typically analog and mixed-signal products have a greater portion of their product cost associated with product testing than digital products. We also operated a semiconductor testing facility to test a portion of our products prior to shipment.

Our current credit terms with our foundry, assembly and testing service providers vary from 30 to 60 days, depending on our relationships with each of them. We generally pay our service providers by direct wire transfer.

We also have made investments in certain of our current suppliers and potential future suppliers, including software developers, foundries and testing service providers. These investments enable us to enhance our business relationships with these suppliers to ensure the adequacy of foundry capacity allocation and quality of services provided to us. We plan to continue to evaluate additional investment opportunities in our supply chain.

### **Competition**

We compete in the market for analog and mixed-signal integrated circuits based on such factors as product performance, power efficiency, new technologies, functional innovation, reliability, price and availability. We believe our principal competitors include Intersil Corporation, Linear Technology Corporation, Maxim Integrated Products, Inc., Monolithic Power Systems, Inc., Ricoh Company, Ltd., Richtek Technology Corporation, Rohm Co., Ltd, Silergy Corporation and Texas Instruments Incorporated. In addition to these competitors, other integrated circuit companies may decide to enter the market with analog and mixed-signal integrated circuit products that compete with our products or incorporate functions similar to those provided by our products.

### **Intellectual Property**

Our intellectual property is primarily developed in-house. We do, from time to time, acquire intellectual property from third parties which we believe is instrumental or complementary to our business. We also license and sell our intellectual property to third parties in exchange for royalties or other consideration. From time to time, we may seek acquisitions to acquire businesses or technologies where synergies exist. Our success depends significantly upon our ability to protect our intellectual property. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy aspects of our products or obtain and use information that we regard as proprietary. Competitors may recruit our employees who have access to our proprietary technologies, processes and operations.

We rely in part on patents to protect our intellectual property. As of December 31, 2016, we had approximately 531 patents issued in the United States and approximately 1,750 patents issued in other countries. In addition, we had approximately 28 patent applications pending in the United States Patent and Trademark Office, and approximately 256 patent applications pending in various countries other than the United States which may or may not be issued. Even if these patents are issued, taken together with our existing patents, they may not be sufficiently broad to protect all of our proprietary rights, or they may prove to be unenforceable. To protect our proprietary rights, we also rely on a combination of copyrights, trademarks, trade secret laws, contractual provisions, licenses and mask work protection under the Federal Semiconductor Chip Protection Act of 1984, and similar laws in other jurisdictions. We also enter into confidentiality agreements with our employees, consultants and customers, and we seek to control access to, and distribution of, our proprietary information. We may from time to time grant rights to third parties for our patents and other intellectual property.

The laws of some foreign countries do not protect our proprietary rights to the same extent as do the laws of the United States, and many companies have encountered substantial infringement problems in these countries, including countries in which we have sold and continue to sell a significant portion of our products. There is a risk that our means of protecting our proprietary rights may not be adequate. For example, our competitors may independently develop similar technology, duplicate our products, or design around our patents and our other intellectual property rights. If we fail to protect our intellectual property adequately, it would make it easier for our competitors to sell competing products. We have several patent, trade secret or copyright litigation matters in Japan, and China.

In Japan, we have one patent litigation matter: *O<sub>2</sub>Micro, Inc. v. Texas Instruments Japan Limited*. In November 2013, we filed a patent infringement suit against Texas Instruments Japan Limited (“Texas Instrument”) in the Civil Division of the Tokyo District Court. The matter was closed in August 2016 with the Court finding no infringement by the defendant on the Japanese patent in question, and we electing not to file an appeal.

In China, we have one patent litigation matters, two trade secret litigation matters, and one copyright litigation matter. *O<sub>2</sub>Micro (China) Co., Ltd. v. Legendsec Information Technology (Beijing) Inc., et al., Chengdu Intermediate Court, China*. We filed a trade secret infringement suit against Yunfeng Li, Chengdu Feitong Technology Co., Ltd. and Legendsec Information Technology (Beijing) Inc. (“Legendsec”) in Chengdu Intermediate Court on August 18, 2014, requesting the three defendants to stop the infringement actions and claim for compensatory damages. Four hearings have been held since October 2014. O<sub>2</sub>Micro (China) and Yunfeng Li reached and signed a settlement agreement on December 29, 2016 and the case has been withdrawn. The matter is now closed. *O<sub>2</sub>Micro (China) Co., Ltd. v. Legendsec Information Technology (Beijing) Inc., Beijing Haidian District People's Court, China*. we filed a copyright infringement suit against Legendsec Information Technology (Beijing) Inc. in Beijing Haidian District People's Court on November 19, 2014, requesting the defendant to stop the infringement actions and claim for compensatory damages. The first hearing was held on March 16, 2015. The second hearing was held on April 22, 2015. The third hearing was held on May 19, 2015. The Court made a judgment to reject our claim on July 3, 2015. We appealed to Beijing Intellectual Property Court on July 14, 2015. The first hearing of the second trial was held on December 23, 2015. The Court made a final judgment to reject our appeal and sustain the original judgment on February 26, 2016. The matter is now closed. *O<sub>2</sub>Micro (China) Co., Ltd. v. Nanjing AnalogChipTech Semiconductor Co., Ltd., et al., Nanjing Intermediate Court, China*. We filed a patent infringement suit against Nanjing AnalogChipTech Semiconductor Co., Ltd., and Nantong Minghui Power Tools Co., Ltd. in Nanjing Intermediate Court on October 29, 2015, requesting two defendants to stop the infringement action, destroy the infringing products and claim for compensatory damages. The first hearing was held on January 18, 2016. All parties reached and signed a settlement agreement on January 18, 2016 and this case is now closed. *O<sub>2</sub>Micro (China) Co., Ltd. v. Nanjing AnalogChipTech Semiconductor Co., Ltd., et al., Nanjing Intermediate Court, China*. We filed a trade secret infringement suit against Xiaohu Tang and Nanjing AnalogChipTech Semiconductor Co., Ltd. in Nanjing Intermediate Court on October 29, 2015, requesting two defendants to stop the infringement action, destroy the infringing products and claim for compensatory damages. The first hearing was held on January 11, 2016. All parties reached and signed a settlement agreement on January 18, 2016 and this case is now closed.

Given the inherent uncertainties in litigation, there cannot be any assurance that we will prevail in any of the pending litigation matters, and we cannot predict the outcome of any such litigation. Litigation is costly, time consuming, and may distract management from other important tasks and, in patent litigation where we are the plaintiff, there is a risk that our patents may be held invalid or unenforceable. In addition, in any litigation arising from claims that we infringe on the intellectual property rights of others, an adverse result could involve an injunction to prevent the sales of a material portion of our products, a reduction or the elimination of the value of related inventories, and the assessment of a substantial monetary award for damages related to past sales, any of which could have a material adverse effect on our result of operations and financial condition.

## ORGANIZATIONAL STRUCTURE

We are incorporated under the laws of the Cayman Islands and we are the parent company for the various subsidiaries that conduct our business on a worldwide basis. As of December 31, 2016, our significant subsidiaries, all of which are wholly-owned, are:

<i>Significant Subsidiary</i>	<i>Country of Incorporation</i>	<i>Date of Incorporation</i>
O <sub>2</sub> Micro, Inc.	U.S.A.	March 1995
O <sub>2</sub> Micro Electronics, Inc.	Taiwan	March 1999
O <sub>2</sub> Micro International Japan Limited	Japan	August 1999
O <sub>2</sub> Micro (Wuhan) Co., Ltd.	China	January 2001
O <sub>2</sub> Micro (Beijing) Co., Ltd.	China	February 2001
O <sub>2</sub> Micro (China) Co., Ltd.	China	April 2001
O <sub>2</sub> Micro (Chengdu) Co., Ltd.	China	July 2004

## PROPERTY, PLANT AND EQUIPMENT

The table below describes our headquarters and the facilities where the above subsidiaries are located as of December 31, 2016:

<b>Location</b>	<b>Approx. Available Square Feet</b>	<b>Lease Expiration</b>
California, USA	37,180	not applicable
Taipei, Taiwan	10,828	2019
Hsinchu, Taiwan	19,632	2017
Tokyo, Japan	1,420	2018
Wuhan, China	14,982	2018
Beijing, China	5,251	2017
Shanghai, China	20,179	not applicable
Chengdu, China	20,011	2017
Grand Cayman, Cayman Islands	600	2017

We maintain our Cayman Islands office to handle corporate affairs, process invoices and receive payments. Research and development, marketing, sales, applications and administrative staff are located in California, USA and China. Marketing, sales, applications, design, worldwide production support, final inspection and shipping, and general and administrative staff are located in Taiwan. We have offices in Japan and Korea for marketing, sales, design, and applications. We believe our current facilities are adequate for our needs for the foreseeable future, and that any additional space required will be available to us on commercially reasonable terms.

In May 2004, we purchased a 37,180 square foot building in California, housing our USA operations. The purchase price was approximately \$4.6 million. In October 2005, we purchased a 30,448 square foot facility in Shanghai, China for approximately \$7.1 million. In April 2006, we purchased 29,935 square foot of undeveloped land in Hsinchu, Taiwan for approximately \$8.8 million. In August 2009, we sold the land in Hsinchu, Taiwan, to a developer in exchange for a pre-sale of a portion of the real estate after it is developed, which will include a portion of an office building and a portion of a parking lot, with a carrying value of approximately \$8.9 million. In the fourth quarter of 2014, a portion of the building units were completed. Considering our current operating scale and capital requirements, we determined to lease out three units to a third party in December 2014. We also sold five building units to third parties since the fourth quarter of 2014. As a result of the sale of building units, net gains of \$767,000 and \$458,000 were recorded for the years ended December 31, 2015 and 2014, respectively. Beginning in November 2015, we have negotiated with a third party company to dispose one of the three units of our office building located in China. A letter of intent has also been signed by both parties in January 2016. We determined that this transaction met the criteria of asset held for sale and such reclassification was made as of December 31, 2015. The transaction was completed in the third quarter of 2016 and a net gain of \$1,725,000 was recorded for the year ended December 31, 2016.

#### ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

#### ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

##### Overview

We design, develop and market high performance integrated circuits for power management components and systems. We also license a limited portion of our proprietary intellectual property to third parties. Our net sales have been derived primarily from the sale of analog and mixed-signal integrated circuit products to customers in the consumer electronics, computer, industrial, communications, and automotive markets.

Our net sales from continuing operations were \$56.6 million in 2016, \$54.8 million in 2015, and \$63.6 million in 2014, respectively. The increase in net sales in 2016 was primarily due to the significant design wins have translated to the meaningful revenue as well as the increase in demand of our power management products for TV, monitors and notebook markets. Although we cannot estimate the extent to which our business will be affected in the future, we anticipate continuing to diversify our customer base and market focus by providing new products that are used in consumer electronics, computer, industrial, communications and automotive markets. Our overall gross margin has fluctuated in the past and is likely to fluctuate in the future due to the stages of our products in their life cycles, variations in our product mix, the timing of our product introductions and specific product manufacturing costs. New products typically have higher gross margins than products that are more mature. Gross margins on the products we sell will typically decline over the life of these products due to competitive pressures and volume pricing agreements.

Operating expenses from continuing operations were \$35.1 million in 2016, \$42.1 million in 2015, and \$49.6 million in 2014. Our operating expenses decreased in 2016 primarily due to our continuous expense reduction efforts to improve our operation effectiveness.

Our net loss from continuing operations was \$3.0 million in 2016, \$21.1 million in 2015, and \$15.1 million in 2014. The significant decrease in net loss from continuing operations in 2016 was primarily due to increased gross profit, decreased operating expenses, the gain on sale of real estate and decreased income tax expenses.

We utilize a fabless semiconductor business model, which means we focus on designing, developing and marketing products, while having these products manufactured by large independent semiconductor foundries. As a fabless semiconductor company, we do not need to invest significant capital to manufacture semiconductor devices, and can take advantage of some of the cost-efficiencies of third-party foundries. We place purchase orders for specific quantities of packaged semiconductor devices or wafers at set prices. We currently use third parties to test and assemble most of our products, which reduces the capital we need to invest in these activities. We also use independent assembly suppliers for the production of our systems security solutions products.

We sell our products through a combination of direct sales offices, sales representatives and distributors. Revenue from product sales to customers, other than distributors, is recognized at the time of shipment, including revenue that has been realized and earned. Sales through distributors are recognized upon shipment to end customers. Under certain conditions, customers may return defective products and we will provide replacements at no charge to the customers for defective products. Allowances for sales returns are provided on the basis of past experience. These provisions are deducted from sales.

## Exit activities

In December 2014, we determined to dissolve our Intelligent Power Group, one of the product lines of our Integrated Circuit Group, which comprised of the IC products such as DC/DC controller ICs, battery charger controllers ICs, charger ICs, and LDO Regulator ICs. The actions taken to dissolve the Intelligent Power Group resulted in significantly reducing the operating activities of the Intelligent Power products and terminating the related workforce. For the year ended December 31, 2014, we recorded costs associated with exit activities of \$3,027,000, of which \$82,000 and \$2,945,000 were related to a loss on asset write-off and one-time employee termination benefits, respectively. We determined that those assets directly held/carried by the Intelligent Power Group provided no future benefit and recognized a loss on asset write-off, including property and equipment of \$24,000 and deferred charges of \$58,000. One-time employee termination benefits of \$2,945,000 were accrued and included in accrued expenses and other current liabilities on the balance sheet as of December 31, 2014 and were settled in 2015. No further transactions were occurred for the year ended December 31, 2016.

## Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States.

The preparation of our consolidated financial statements requires us to make estimates and judgments that affect the reported amount of assets, liabilities, net sales and expenses, and related disclosure of contingent assets and liabilities. We evaluate our estimates on an ongoing basis, including those related to valuation allowance for deferred tax assets, allowance for doubtful accounts, inventory valuation, useful lives for property and equipment, impairment of long-lived assets, contingencies, fair value, other-than-temporary impairment of securities, allowance for sales returns, uncertain tax liabilities, and stock-based compensation. We base our estimates and judgments on our historical experience, knowledge of current conditions and our beliefs of what could occur in the future considering available information. Because our estimates may vary in each situation, our actual results may differ from our estimates under different assumptions and conditions.

Our management considers the following factors in reviewing our financial statements:

- the selection of critical accounting policies; and
- the judgments and other uncertainties affecting the application of those critical accounting policies.

The selection of critical accounting policies, the judgments and other uncertainties affecting the application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing our financial statements. Our principal accounting policies are set forth in detail in Note 2 to our consolidated financial statements included elsewhere in this Annual Report.

We believe the following critical accounting policies affect our more significant judgments used in the preparation of our financial statements.

## Revenue Recognition and Accounts Receivable Allowances

We recognize revenue on sales to direct customers in accordance with four basic criteria must be met before revenue can be recognized: (1) persuasive evidence of an agreement exists, (2) delivery has occurred or services have been rendered, (3) the fee is fixed and determinable, and (4) collectability is reasonably assured. Determination of criteria (3) and (4) is based on management's judgments regarding the ability to estimate returns and the collectability of those fees.

In certain limited instances, we sell products through distributors. Since the title and risk have not been transferred upon shipment to distributors, we recognize revenues on these sales only when these distributors sell the products. In addition, products held by these distributors are included in our inventory balance. Accounts receivable from these distributors are recognized and inventory is relieved upon shipment to end customers as title to inventories generally transfers upon shipment.

We make allowances for future product returns at the time revenue is recognized. We analyze historical returns, changes in current demand and acceptance of products when evaluating the adequacy of such allowances. Estimates may differ from actual product returns and allowances and these differences may materially affect our reported revenue and amounts ultimately collected on accounts receivable. In addition, we monitor collectability of accounts receivable primarily through review of the accounts receivable aging. When facts and circumstances indicate the collection of specific amounts or from specific customers is at risk, we assess the impact on amounts recorded for bad debts and, if necessary, will record a charge in the period such determination is made. To date, we have not experienced material write-offs of accounts receivable due to uncollectability.

## Inventories

Our inventories are stated at the lower of standard cost or market value. Cost is determined on a currently adjusted standard basis, which approximates actual cost on a first-in first-out basis. Because of the cyclical nature of the market, inventory levels, obsolescence of technology and product life cycles, we write down inventories to net realizable value based on backlog, forecasted product demand and historical sales levels. Backlog is subject to revisions, cancellations and rescheduling. Actual demand and market conditions may be lower than those projected by us. This difference could have a material adverse effect on our gross margin should additional inventory write downs become necessary. For the years ended December 31, 2016, 2015, and 2014, inventory write-downs were \$1.5 million, \$913,000, and \$1.5 million, respectively.



## Long-term Investments

Long-term investments in private companies over which we do not exercise significant influence are accounted for under the cost method. Management evaluates related information in determining whether an other-than-temporary decline in value exists. Factors indicative of an other-than-temporary decline include recurring operating losses, credit defaults and subsequent rounds of financing at an amount below the cost basis of the investment. The list is not all-inclusive and management periodically weighs all quantitative and qualitative factors in determining if any impairment loss exists. Long-term investments are measured and recorded at the fair value if an impairment loss is recognized. We use the best and most relevant data available and the acceptable valuation model, such as a discounted cash flow model or net asset value per share, to determine the fair value of impaired investment. For the year ended December 31, 2016, no impairment charges were recorded. For the year ended December 31, 2015, impairment losses of \$4,953,000 were recorded on our investments in Sigurd Microelectronics (Cayman) Co., Ltd. and Philip Ventures Enterprise Fund. For the year ended December 31, 2014, an impairment loss of \$83,000 was recorded on our investment in Verticil Electronics Corp. Please refer to the discussions in note 9 to the consolidated financial statements.

Long-term investments in listed companies are classified as available-for-sale securities and are recorded at fair value. Unrealized gains and losses on these investments are included in accumulated other comprehensive income and loss as a separate component of shareholders' equity, net of any related tax effect, unless unrealized losses are deemed other-than-temporary. Unrealized losses are recorded as a charge to income when deemed other-than-temporary.

## Long-Lived Assets

We perform periodic reviews to determine whether facts and circumstances exist that would indicate that the carrying amounts of long-lived assets might not be fully recoverable. If facts and circumstances indicate that the carrying amount of long-lived assets might not be fully recoverable, we compare projected undiscounted net cash flows associated with the related assets over their estimated remaining useful life against their respective carrying amounts. In the event that the projected undiscounted cash flows are not sufficient to recover the carrying value of the assets, the assets are written down to their estimated fair values based on the expected discounted future cash flows attributable to the assets. Evaluation of impairment of long-lived assets requires estimates in the forecast of future operating results that are used in the preparation of the expected future undiscounted cash flows. Actual operating results and remaining economic lives of the long-lived assets could differ from the estimates used in assessing the recoverability of these assets. These differences could result in additional impairment charges, which could have a material adverse impact on the results of operations. For the year ended December 31, 2014, a loss on asset write-off related to the exit activities was approximately \$82,000, including property and equipment of \$24,000 and deferred charges of \$58,000. For the years ended December 31, 2016 and 2015, no impairment charges were recorded.

## Income Taxes

The provision for income tax represents income tax paid and payable for the current year plus the changes in the deferred income tax assets and liabilities during the year. Deferred income tax assets are primarily the tax effects of the operating loss carry-forwards, research and development credit carry-forwards and temporary differences. On a periodic basis we evaluate the deferred tax assets balance for realizability. To the extent we believe it is more likely than not that some portion of deferred tax assets will not be recognized, we will increase the valuation allowance against the deferred tax assets. Realization of the deferred tax assets is dependent primarily upon future taxable income, changes in tax laws and other factors. These changes, if any, may require possible material adjustment to the deferred tax assets, resulting in a reduction in net income in the period when such determinations are made. The valuation allowance as of December 31, 2016 and 2015 was \$6.3 million and \$6.2 million, respectively. The valuation allowance increased by \$18,000 and \$13,000 for the years ended December 31, 2016 and 2015, respectively. The changes in the valuation allowance were primarily due to the fluctuations in R&D credits from O<sub>2</sub>Micro, Inc. that could not be utilized. We adopt a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than 50% likely of being realized upon ultimate settlement.

We evaluate our future growth phase and working capital requirements of each entity in the group in the foreseeable future to consider the repatriation of earnings from subsidiaries of reinvestment of undistributed earnings. No incomes taxes expense and deferred taxes liabilities will be accrued by us if we plan to reinvest undistributed earnings of subsidiaries. However, on the other hand, if we plan to remit the undistributed earnings of subsidiaries, the accrual will be made based on our intention. Before the year of 2015, we planned to reinvest the undistributed earnings of all subsidiaries and did not accrue any income tax expense and deferred taxes liabilities. In the year of 2015, to better position ourselves for the future growth phase, we considered to remit the undistributed earnings of subsidiaries in Taiwan and China. As a result, deferred tax liabilities from withholding tax for the unremitted earnings in Taiwanese and Chinese subsidiaries have been recorded for \$920,000 and \$2,188,000 as of December 31, 2016 and 2015, respectively.

## Legal Contingencies

We are currently involved in various claims and legal proceedings. We periodically assess each matter in order to determine if a contingent liability should be recorded. In making the determination, we may, depending on the nature of the matter, consult with external counsel and technical experts. Based on the information obtained combined with our judgment regarding all the facts and circumstances of each matter, we reserve the right to determine whether it is probable that a contingent loss may be incurred and whether the amount of such loss can be estimated. Should a loss be probable and estimable, we will record a contingent loss by taking into consideration the advice received from experts in the specific matter, current status of legal proceedings, prior case history and other factors. Should the judgments and estimates be incorrect, we may need to record additional contingent losses that could materially adversely impact our results of operations.

## Stock-based compensation

We grant stock options to our employees and certain non-employees, and we estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense ratably over the requisite service periods. We have elected to use the Black-Scholes option pricing model to determine the fair value of stock options on the date of grant. The option pricing module requires the input of highly subjective assumptions, including the expected stock price volatility, risk-free interest rate and expected option life, and by estimated option shares to be vested at the end of the vesting schedule. We also grant restricted stock units (“RSU”) to our employees and the RSU are measured based on the fair market value of the underlying stock on the dates of grant.

## Fair Value Measurements

We measure our cash equivalents and marketable securities at fair value. We also determine the fair value of long-term investments and long-lived assets whenever events or changes in circumstances indicate the carrying value may not be recoverable. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value:

Level 1 – Observable inputs such as quoted prices for identical instruments in active markets;

Level 2 – Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly;

Level 3 – Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

## Recent Accounting Pronouncements

Please refer to the discussions in note 2 to the consolidated financial statements.

## Operating Results

The following table summarizes historical results of operations as a percentage of net sales from continuing operations for the periods shown.

	Years Ended December 31		
	2016	2015	2014
<b>Consolidated Statement of Operations Data:</b>			
Net sales	100.0%	100.0%	100.0%
Cost of sales	48.3	49.5	48.5
Gross margin	51.7	50.5	51.5
Operating expenses:			
Research and development	27.7	33.7	34.4
Selling, general and administrative	34.4	43.1	38.8
Cost associated with exit activities	-	-	4.8
Litigation income	-	-	(0.1)
Total operating expenses	62.1	76.8	77.9
Loss from operations	(10.4)	(26.3)	(26.4)
Non-operating income (loss)–net	7.0	(3.7)	4.6
Income tax expense	1.9	8.5	1.9
Net loss from continuing operations	(5.3)	(38.5)	(23.7)
Loss from discontinued operations, net of tax	-	-	-
Net loss	(5.3)%	(38.5)%	(23.7)%

The following table sets forth the breakdown of our net sales from continuing operations by product category for the periods shown:

	Years Ended December 31		
	2016	2015	2014
	<i>(in thousands)</i>		
<b>Integrated Circuits:</b>			
Mixed-signal	\$ 40,866	\$ 39,268	\$ 46,486
Analog	15,623	15,213	16,600
Digital	65	-	67
<b>Licensed Intellectual Property</b>	7	360	438
<b>Total</b>	<u>\$ 56,561</u>	<u>\$ 54,841</u>	<u>\$ 63,591</u>

## Years Ended December 31, 2016 and 2015.

*Net Sales.* Net sales from continuing operations consisted of product revenues generated principally by sales of our integrated circuit products. Net sales from continuing operations for the year ended December 31, 2016 were \$56.6 million, an increase of \$1.7 million or 3.1% from \$54.8 million for the year ended December 31, 2015, which primarily resulted from the significant design wins translating to the meaningful revenue as well as the increase in demand of our power management products for TV, monitors and notebook markets. In 2016, net sales from our mixed-signal integrated circuit products were \$40.9 million, an increase of \$1.6 million or 4.1% from \$39.3 million in 2015, which primarily resulted from the increase in demand of our power management products for notebook, monitors, and TV markets. In 2016, net sales from analog integrated circuit products were \$15.6 million, only a small increase of \$410,000 or 2.7% from \$15.2 million in 2015. Net sales from our digital integrated circuit products were \$65,000 in 2016, an increase of \$65,000 or 100% from \$0 in 2015, which resulted primarily from no incidental sales of our CardBus controller products in 2015. Net sales from our licensed intellectual property were \$7,000 in 2016, a decrease of \$353,000 or 98.1% from \$360,000 in 2015, which primarily resulted from the expiration of a license agreement with a third party in November 2015.

*Gross Profit.* Gross profit from continuing operations represents net sales less cost of sales. Cost of sales primarily consists of the costs of purchasing packaged integrated circuit products manufactured and assembled for us by independent foundries and packaging vendors and other costs associated with the procurement, storage and shipment of these products. Gross profit from continuing operations for the year ended December 31, 2016, was \$29.2 million, an increase of \$1.5 million or 5.6% from \$27.7 million for the year ended December 31, 2015. This increase was primarily due to the increased sales in our integrated circuit products in 2016. Gross profit from continuing operations as a percentage of net sales for the year ended December 31, 2016, increased to 51.7% from 50.5% for the year ended December 31, 2015, primarily due to the product mix of sales of new products with higher gross margins. We expect that our gross profit as a percentage of net sales will continue to fluctuate in the future as a result of the stages of our products in their life cycles, variations in our product mix, the timing of our product introductions and specific product manufacturing costs.

*Research and Development Expenses.* Research and development expenses from continuing operations consist primarily of salaries and related costs of employees engaged in research, design and development activities and, to a lesser extent, expenses for engineering expenses (e.g. one-time pilot run, engineering sample, tooling, and testing expenses). Research and development expenses for the year ended December 31, 2016, were \$15.6 million, a decrease of \$2.8 million or 15.4% from \$18.5 million for the year ended December 31, 2015. The decrease primarily resulted from decreased engineering expenses associated with design and development of new products. As a percentage of net sales, research and development expenses were 27.7% for the year ended December 31, 2016, a decrease from 33.7% for the year ended December 31, 2015. Research and development expenses as a percentage of net sales will fluctuate from quarter to quarter depending on the amount of net sales and the success of new product development efforts, which we view as critical to our future growth. At any point in time, we may also have internal research and development projects underway, which may or may not lead to new product designs. We expect to continue the development of innovative technologies and processes for new products and we believe that a continued commitment to research and development is essential in order to maintain the competitiveness of our existing products and to provide innovative new product offerings. Therefore, we expect to continue to invest significant resources in research and development in the future.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses from continuing operations consist primarily of employee-related expenses, office facilities costs, promotional expenses, and travel expenses. Selling, general and administrative expenses for the year ended December 31, 2016, were \$19.5 million, a decrease of \$4.2 million or 17.6% from \$23.6 million for the year ended December 31, 2015. This decrease was primarily due to our continued cost-cutting effort implemented. As a percentage of net sales, selling, general and administrative expenses were 34.4% for the year ended December 31, 2016, a decrease from 43.1% for the year ended December 31, 2015.

*Litigation Income.* Litigation income consists primarily of amounts received from settlement, damage awards, and award of costs or related interest. Litigation income for the year ended December 31, 2016 was \$23,000. There was no litigation income for the year ended December 31, 2015.

*Non-operating Income (losses)-net.* Non-operating income (loss)-net from continuing operations reflects primarily interest earned on cash and cash equivalents and short-term investments, foreign exchange transaction gains or losses, impairment loss on long-term investments, and disposal gain on sale of long-term investments and real estate. Non-operating income-net was \$3.9 million for the year ended December 31, 2016, an increase of \$6.0 million from non-operating loss-net of \$2.0 million for the year ended December 31, 2015, primarily due to the increased gain on sale of real estates, no occurrence of impairment loss on long-term investments, and increased gain on sale of long-term investments.

*Income Tax Expense.* Income tax expense from continuing operations was \$1.1 million for the year ended December 31, 2016, a decrease of \$3.6 million from \$4.6 million for the year ended December 31, 2015, primarily due to the decreased withholding taxes on repatriation of profits from subsidiaries in Taiwan and China.

#### **Years Ended December 31, 2015 and 2014.**

*Net Sales.* Net sales from continuing operations consisted of product revenues generated principally by sales of our integrated circuit products. Net sales from continuing operations for the year ended December 31, 2015 were \$54.8 million, a decrease of \$8.8 million or 13.8% from \$63.6 million for the year ended December 31, 2014, which primarily resulted from the overall weak macro-economic factors that lead to the decrease in demand of our power management products for TV, monitors and notebook markets. The decrease in net sales was also resulted from the slower than anticipated growth from our new products for the tablet and smartphone markets. In 2015, net sales from our mixed-signal integrated circuit products were \$39.3 million, a decrease of \$7.2 million or 15.5% from \$46.5 million in 2014, which primarily resulted from the decrease in demand of our power management products for notebook, monitors, and TV markets. In 2015, net sales from analog integrated circuit products were \$15.2 million, only a small decrease of \$1.4 million or 8.4% from \$16.6 million in 2014, which resulted primarily from the continued weak demand by several of our major notebook customers, partially offset by the increase sales in our battery management products. Net sales from our digital integrated circuit products were \$0 in 2015, a decrease of \$67,000 or 100% from \$67,000 in 2014, which resulted primarily from no incidental sales of our CardBus controller products in 2015. Net sales from our licensed intellectual property were \$360,000 in 2015, a decrease of \$78,000 or 17.8% from \$438,000 million in 2014, which primarily resulted from decreased shipments of third party's products which are licensed with our intellectual property.

*Gross Profit.* Gross profit from continuing operations represents net sales less cost of sales. Cost of sales primarily consists of the costs of purchasing packaged integrated circuit products manufactured and assembled for us by independent foundries and packaging vendors and other costs associated with the procurement, storage and shipment of these products. Gross profit from continuing operations for the year ended December 31, 2015, was \$27.7 million, a decrease of \$5.0 million or 15.4% from \$32.7 million for the year ended December 31, 2014. This decrease was primarily due to the decreased sales in our integrated circuit products in 2015. Gross profit from continuing operations as a percentage of net sales for the year ended December 31, 2015, decreased to 50.5% from 51.5% for the year ended December 31, 2014, primarily due to the product mix of sales of products with low gross margins. We expect that our gross profit as a percentage of net sales will continue to fluctuate in the future as a result of the stages of our products in their life cycles, variations in our product mix, the timing of our product introductions and specific product manufacturing costs.

*Research and Development Expenses.* Research and development expenses from continuing operations consist primarily of salaries and related costs of employees engaged in research, design and development activities and, to a lesser extent, expenses for engineering expenses (e.g. one-time pilot run, engineering sample, tooling, and testing expenses). Research and development expenses for the year ended December 31, 2015, were \$18.5 million, a decrease of \$3.4 million or 15.5% from \$21.9 million for the year ended December 31, 2014. The decrease primarily resulted from reduced number of employees and decreased engineering expenses associated with design and development of new products. As a percentage of net sales, research and development expenses were 33.7% for the year ended December 31, 2015, a decrease from 34.4% for the year ended December 31, 2014. Research and development expenses as a percentage of net sales will fluctuate from quarter to quarter depending on the amount of net sales and the success of new product development efforts, which we view as critical to our future growth. At any point in time, we may also have internal research and development projects underway, which may or may not lead to new product designs. We expect to continue the development of innovative technologies and processes for new products and we believe that a continued commitment to research and development is essential in order to maintain the competitiveness of our existing products and to provide innovative new product offerings. Therefore, we expect to continue to invest significant resources in research and development in the future.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses from continuing operations consist primarily of employee-related expenses, office facilities costs, promotional expenses, and travel expenses. Selling, general and administrative expenses for the year ended December 31, 2015, were \$23.6 million, a decrease of \$1.1 million or 4.4% from \$24.7 million for the year ended December 31, 2014. This decrease was primarily due to reduced number of employees as well as our continued cost-cutting effort implemented. As a percentage of net sales, selling, general and administrative expenses were 43.1% for the year ended December 31, 2015, an increase from 38.8% for the year ended December 31, 2014.

*Cost associated with exit activities.* Cost associated with exit activities consisted primarily of one-time asset write-off charges and employee termination benefits associated with our dissolution activities of Intelligence Power Group in 2014. There was no cost associated with exit activities for the year ended December 31, 2015.

*Litigation Income.* Litigation income consists primarily of amounts received from settlement, damage awards, and award of costs or related interest. There was no litigation income for the year ended December 31, 2015.

*Non-operating Income (losses)-net.* Non-operating income (loss)-net from continuing operations reflects primarily interest earned on cash and cash equivalents and short-term investments, foreign exchange transaction gains or losses, impairment loss on long-term investments, and disposal gain on sale of long-term investments and real estate. Non-operating loss-net was \$2.0 million for the year ended December 31, 2015, a decrease of \$5.0 million from non-operating income-net of \$3.0 million for the year ended December 31, 2014, primarily due to the incurrence of impairment loss on our long-term investments.

*Income Tax Expense.* Income tax expense from continuing operations was \$4.6 million for the year ended December 31, 2015, an increase of \$3.5 million from \$1.2 million for the year ended December 31, 2014, primarily due to the withholding taxes on repatriation of profits from subsidiaries in Taiwan and China.

### **Liquidity and Capital Resources**

Since our inception, we have financed our operations primarily through private sales of securities and through our initial public offering in August 2000, and our public offering in November 2001, as well as cash provided by operating activities prior to 2012. Cash, cash equivalents, and short-term investments were in a total of \$52.9 million at December 31, 2016, as compared to \$52.4 million at December 31, 2015. Our operating activities generated cash outflows in the amount of \$7.8 million, \$8.6 million and \$10.3 million in the years ended December 31, 2016, 2015, and 2014, respectively.

Non-cash charges primarily consist of depreciation of property and equipment, amortization of stock-based compensation, gain on sale of long-term investments, loss on asset write-off, gain on disposal of property and equipment, impairment charges related to long-term investments, inventory write-downs, and changes of deferred income tax assets and liabilities. The working capital components that have a significant impact on our cash flows are accounts receivable, inventories, notes and accounts payable, prepaid expenses and other current assets, deferred charges, and accrued expense and other current liabilities.

Net cash inflows/outflows from operations resulted from net income/loss adjusted by non-cash changes and changes in inventories, accounts receivable, notes and accounts payable, accrued expenses and other current liabilities, income tax payable, and other liabilities. For the year ended December 31, 2016, net cash used in operating activities was \$7.8 million, primarily from our operating results during the year, an increase in accounts receivables, an increase in inventories, an increase in deferred charges, a decrease in income tax payable, and a decrease in accrued expenses and other current liabilities, partially offset by an increase in notes and accounts payable. For the year ended December 31, 2015, net cash used in operating activities was \$8.6 million, primarily from our operating results during the year, an increase in inventories, an increase in deferred charges, and a decrease in accrued expenses and other current liabilities, partially offset by a decrease in accounts receivable, an increase in note and accounts payable, and an increase in income tax payable. For the year ended December 31, 2014, net cash used in operating activities was \$10.3 million, primarily from our operating results during the year, an increase in inventories, a decrease in notes and accounts payable, and an increase in deferred charges, partially offset by a decrease in accounts receivable.

In 2016, we had a net cash outflow from investing activities of \$1.3 million as compared to a net cash inflow of \$12.9 million in 2015. This net cash used in investing activities in 2016 was principally due to the net acquisition of short-term investments of \$10.5 million, the sale of long-term investments of \$6.0 million, and the disposal of property and equipment of \$3.8 million, offset by the acquisition of property and equipment of \$673,000 and the net acquisition of short-term investments of \$10.5 million. In 2015, we had a net cash inflow from investing activities of \$12.9 million as compared to a net cash inflow of \$14.4 million in 2014. This net cash provided by investing activities in 2015 was principally due to the net sale of short-term investments of \$9.6 million, and the disposal of property and equipment of \$3.2 million, offset by the acquisition of property and equipment of \$724,000. In 2014, we had a net cash inflow from investing activities of \$14.4 million. This net cash provided by investing activities in 2014 was principally due to the net sale of short-term investments of \$12.0 million, the sale of long-term investments of \$1.3 million, and the disposal of property and equipment of \$2.0 million, offset by the acquisition of property and equipment of \$1.0 million.

Net cash outflow from our financing activities in 2016 was \$544,000 which was primarily due to the repurchase of \$619,000 of our shares under a share repurchase program, partially offset by proceeds of \$75,000 from the exercise of stock options and issuance of shares under our existing employee stock purchase plan for the year. Net cash outflow from our financing activities in 2015 was \$3.0 million which was primarily due to the repurchase of \$3.2 million of our shares under a share repurchase program, partially offset by proceeds of \$211,000 from the exercise of stock options and issuance of shares under our existing employee stock purchase plan for the year. Net cash outflow from our financing activities in 2014 was \$4.7 million which was primarily due to the repurchase of \$5.0 million of our shares under a share repurchase program, partially offset by proceeds of \$302,000 from the exercise of stock options and issuance of shares under our existing employee stock purchase plan for the year. We believe our liquidity provided by existing cash, cash equivalents balances and short-term investments will be sufficient to meet our capital requirements for at least the next 12 months. We are also in the process of monetizing some of our real-estate assets and long-term investments to enhance our capital resources and continue to monitor and reduce our operating spending seriously. We incurred capital expenditures of \$673,000, \$724,000, and \$1.0 million in 2016, 2015, and 2014, respectively. Our future capital expenditure requirements will depend on many factors, including the inventory levels we maintain, the level of investments we make in new technology and improvements to existing technology, the levels of promotion and advertising required to launch new products and attain a competitive position in the marketplace, and the market acceptance of our products. Thereafter, we may need to raise additional funds through public or private financing. No assurance can be given that additional funds will be available or that we can obtain additional funds on terms favorable to us.

### **Research and Development, Patents and Licenses, etc.**

We believe that the continued introduction of new products in our target markets is essential to our growth. As of December 31, 2016, we had approximately 202 full-time employees world-wide engaged in research and development efforts. Our total expenditures for research and development were \$15.6 million, \$18.5 million, and \$21.9 million for the years ended December 31, 2016, 2015, and 2014, respectively.

We employ designers who are experienced in system architecture, analog, mixed signal and software design and development. We also utilize independent contractors from time-to-time for specific research and development projects. Our internal research and development personnel thoroughly review the external development processes and the design of these products as part of our quality assurance process. All development is carried out using ISO 9001 and ISO 14001 certified design processes, and our design tools are continuously enhanced to improve design, fabrication and verification of our products.

Our research and development activities are a constantly evolving process which reflects the results of our ongoing projects, our expectations regarding market developments and changes in customer demand and industry specifications. We commence new projects or alter the scope or direction of existing projects on a regular basis under the guidance of our management and senior research personnel.

We work with our customers to monitor the performance of our product designs and to provide support at each stage of customer product development. Due to the complexity of our products, we maintain a significant direct applications support staff for customer technical support in our key markets including in Taiwan and China. These direct applications engineering personnel assist with supporting existing products at key customers. Additionally, we work closely with our customers to develop highly efficient power management products for specific applications.

#### Trend Information

See “Risk Factors” and “Operating and Financial Review and Prospects” above.

#### Off-Balance Sheet Arrangements

There are no off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

#### Tabular Disclosure of Contractual Obligations

The table below describes our contractual obligations as of December 31, 2016:

Contractual Obligations	Payments due by period				
	Total	Less than 1 year	1-3 years <i>(in thousands)</i>	3-5 years	More than 5 years
Operating lease obligations	\$ 1,842	\$ 1,216	\$ 558	\$ 68	\$ -
Licenses, maintenance and support	275	236	39	-	-
Pension	474	13	35	56	370
Total	<u>\$ 2,591</u>	<u>\$ 1,465</u>	<u>\$ 632</u>	<u>\$ 124</u>	<u>\$ 370</u>

#### ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

##### Directors and Senior Management

Our executive officers and directors and their ages as of December 31, 2016, were as follows:

Name	Age	Position
Sterling Du	57	Chief Executive Officer, Class I Director and Chairman of the Board
Chuan Chiung “Perry” Kuo	57	Chief Financial Officer, Joint Secretary and Class I Director
James Keim	72	Class II Director and Head of Marketing and Sales
Michael Austin	81	Independent Non-executive Director, Class III Director, Chairman of the Nominating committee and member of Compensation Committee
Lawrence Lin	66	Independent Non-executive Director, Class II Director, Chairman of the Compensation Committee and member of Audit Committee
Ji Liu	81	Independent Non-executive Director, Class II Director
Teik Seng Tan	62	Independent Non-executive Director, Class I Director and Chairman of Audit Committee
Daniel Lenehan	61	Independent Non-executive Director, Class III Director and member of the Audit Committee
Vijay Kumar	54	Independent Non-executive Director and Class III Director and member of the Nominating Committee

Our Class I Directors have held office from the date of the annual general meeting in 2014 for a three year term until 2017; our Class II Directors have held office from the date of the annual general meeting in 2015 for a three year term until 2018; and our Class III Directors have held office from the date of the annual general meeting in 2016 for a three year term until 2019.

#### *Executive Directors*

*Sterling Du* has served as our chief executive officer and chairman of our board of directors since March 1997 and as a Class I Director since June 2001. He also served as our chief financial officer from March 1997 to March 1999. From May 1995 to March 1997, Mr. Du was president and chief executive officer of O<sub>2</sub>Micro, Inc., our predecessor entity. From October 1993 to April 1995, Mr. Du was vice president of engineering at GreenLogic, Inc., a semiconductor design company, which he co-founded. Mr. Du received a B.S. in chemical engineering from National Taiwan University and an M.S. in electrical engineering from the University of California, Santa Barbara.

*Chuan Chiung "Perry" Kuo* has served as our general manager of Taiwan operations since January 1997, as chief financial officer and a director since March 1999, as secretary since October 1999 and as a Class I director since June 2001. From February 1992 to December 1996, he was executive vice president of Pac Net Group, a holding company with investments in chemicals, electronics and real estate. From July 1983 to February 1992, he held various positions at Formosan Rubber Group, a rubber manufacturer, including product design engineer, plant manager, research and development director, and vice president. Mr. Kuo received a B.S. in chemical engineering from National Taiwan University and an M.B.A. from the Rotterdam School of Management, Erasmus University in The Netherlands.

*James Keim* has served as a director since March 1999 and as Head of Marketing and Sales since December 2001 and a Class II director since June 2001. He also served as our chief operating officer from June 1998 to June 2001. From March 1995 to June 1998, Mr. Keim was a principal in Global Marketing Associates, an international consulting firm. Prior to March 1995, he had been vice president of sales at Alliance Semiconductor Corporation, vice president of marketing at Performance Semiconductor Corporation and worldwide linear marketing manager at Fairchild Semiconductor Corporation. Mr. Keim received a B.S. in engineering from Iowa State University, an M.S. in electrical engineering and an M.B.A. from the University of Illinois.

#### *Independent Non-Executive Directors*

*Michael Austin* has served as a director since October 1997 and as a Class III director since June 2001. He currently serves as chairman of the nominating committee and member of the compensation committee. Mr. Austin is a resident of the Cayman Islands and is a Chartered Accountant. He was admitted as a Fellow of The Institute of Chartered Accountants in England and Wales in 1974. He is an Associate Member of The Chartered Institute of Taxation, a Member of the Society of Trust and Estate Practitioners, a Member of the Cayman Islands Society of Professional Accountants, a Member of the Cayman Islands Institute of Directors, and a Notary Public of the Cayman Islands. Mr Austin served as the managing partner of the Cayman Islands office of KPMG Peat Marwick, an international accounting firm, for 23 years. Since retiring in July, 1992 Mr Austin has been a consultant and currently serves as non-executive director on several company boards, including those of a number of mutual funds, hedge funds, structured investment vehicles, trust and insurance companies. Mr Austin served as a director of the Cayman Islands Monetary Authority from January 1997 and was appointed Chairman of the Monetary Authority in January 2003, a position he held until his retirement on July 31, 2004. He has also served on a variety of other government committees and government related boards, and is currently Chairman of the Auditors Oversight Authority, a Cayman Islands Statutory Board. In 1990 Mr Austin was awarded an M.B.E. by Her Majesty the Queen in recognition of services to the public and business community.

*Lawrence Lin* has served as a Class II Director, member of the audit committee and chairman of the compensation committee since June 2003. He is a Certified Public Accountant in Taiwan. Since 1990, Mr. Lin has been a partner of UHY L&C Company, Certified Public Accountants, which is an independent member firm of Urbach Hacker Young International. Mr. Lin was a director of Urbach Hacker Young International from October 1994 to October 1998. Prior to UHY L&C Company, he was a partner at T N Soong & Co. Mr. Lin serves as corporate supervisor and chairman of the audit committee of Yageo Corporation, which is a Taiwan listed public company. He graduated from Taipei Vocational Commercial School in 1969.

*Ji Liu* has served as a Class II Director since June 2007. Mr. Liu has been an Honorary President of the China Europe International Business School since 2005. He has been the Chairman of China Europe International Business School Education Development Foundation since 2005. From 1999 to 2004, Mr. Liu was Executive President and President of the China Europe International Business School. From 1993 to 1999, Mr. Liu was a Research Fellow, Member of the Academic Board, Graduate Supervisor and Deputy Chairman of the Chinese Academy of Social Sciences. He received a B.S. in power mechanical engineering from Tsinghua University in China.

*Teik Seng Tan* has served as a Class I Director and a member of audit committee since June 2008. Mr. Tan has served as Chairman of the audit committee since 2010. Mr. Tan was previously employed by AMD Singapore Pte Ltd. from 1984 to 2007 where he held various positions, the last position being Senior Executive Managing Director. He is also a member of the Board of Directors for Bizlink Centre Singapore Ltd since 1999. He also has been Chairman of the Board of Directors for Bizlink Centre Singapore Ltd. from 2001 to 2010. Mr. Tan is a member of the Advisory Council for the Singapore Human Resource Institute and a member of the Advisory Council of the School of Engineering at Temasek Polytechnic. Mr. Tan received a B.E. in Electrical Engineering from the National University of Singapore and an M.S. in Industrial Engineering from the National University of Singapore. He is also a Fellow of the Singapore Human Resource Institute.

*Daniel Lenehan* has served as a Class III Director and a member of the audit committee since June, 2016. Mr. Lenehan brings to O2Micro's Board of Directors more than thirty years of experience in semiconductor product development, technical marketing, foundry management and engineering experience at a wide variety of technology companies in various Director and VP level positions. Mr. Lenehan was one of the key contributors to Intel's expansion of the notebook market by assuming a number of Director roles including leadership positions in the areas of systems development, industry initiatives, mobile architecture, chipset design and R&D labs. As VP of Engineering at Xilinx Corp, Mr. Lenehan led the Spartan Field Programmable Gate Array development team responsible for architecture, design, layout, product and test engineering across North America, Ireland, and Asia. Mr. Lenehan has a BSEE from the New Jersey Institute of Technology.

*Vijay Kumar* has served as a Class III Director and a member of the nominating committee since December 2016. Mr. Kumar is currently the Nemirovsky Family Dean of Penn Engineering and been a faculty member at the University of Pennsylvania since 1987. Mr. Kumar has held many administrative positions in the School of Engineering and Applied Science, including director of the GRASP Laboratory, chair of Mechanical Engineering and Applied Mechanics, and the position of the Deputy Dean. Mr. Kumar is a fellow of ASME and IEEE and a member of the National Academy of Engineering and Mr. Kumar has also served as the assistant director of robotics and cyber physical systems at the White House Office of Science and Technology Policy. Mr. Kumar received his Bachelor of Technology degree from the Indian Institute of Technology, Kanpur and his Ph.D. from Ohio State University in 1987.

There are no family relationships among any of our directors or executive officers. There are no arrangements or understandings with major shareholders, customers, suppliers or others, pursuant to which any person referred to above was selected as a director or member of senior management.

### **Compensation**

We paid an aggregate amount of compensation during 2016 to our directors and members of our administrative, supervisory or management bodies as a group equal to approximately \$2.1 million. All of our officers and directors are eligible to participate in our employee benefit plans except non-employee directors are not eligible to participate in our employee stock purchase plan.

### **Share Ownership of Directors and Senior Management**

As of December 31, 2016, the aggregate number of ordinary shares beneficially owned by our directors and members of our administrative, supervisory or management bodies was 206,878,400. This number includes options to purchase an aggregate of 94,050,950 ordinary shares under our, 1999 Stock Plan and 2005 Share Option Plan and 2015 Share Incentive Plan exercisable within 60 days of December 31, 2016.

### **Employee Benefit Plans**

*1997 Stock Plan.* Our 1997 stock plan ("1997 Stock Plan") was adopted by our board of directors and approved by our shareholders in 1997. The 1997 Stock Plan provides for the granting to our employees of incentive stock options within the meaning of Section 422 of the United States Internal Revenue Code, and for the granting to employees and independent contractors of nonstatutory stock options and stock purchase rights. Our board of directors and our shareholders authorized a total of 3,700,000 ordinary shares for issuance pursuant to the 1997 Stock Plan, as amended or 185,000,000 ordinary shares after taking into account the 50-to-1 stock split on November 25, 2005. No more grants have been made under this plan after the consummation of our initial public offering on August 23, 2000. Our 1997 Stock Plan was terminated effective on March 2, 2006, the date of the listing of our ordinary shares on the SEHK; provided that options granted under the plan remain outstanding in accordance with their terms.

*1999 Stock Incentive Plan.* Our 1999 stock incentive plan ("1999 Stock Incentive Plan") was adopted by our board of directors in October 1999 and was approved by our shareholders prior to the consummation of our initial public offering in August 2000. The 1999 Stock Incentive Plan provides for the granting to employees of incentive stock options within the meaning of Section 422 of the Internal Revenue Code and the granting of nonstatutory stock options, stock appreciation rights, dividend equivalent rights, restricted stock, performance units, performance shares and other equity-based rights to our employees, directors and consultants. Initially, we have reserved 3,000,000 ADSs for issuance under the 1999 Stock Incentive Plan or 150,000,000 ordinary shares after taking into account the 50-to-1 stock split on November 25, 2005. Commencing January 1, 2001, the number of ordinary shares of stock reserved for issuance under the 1999 Stock Incentive Plan would be increased annually by a number equal to 4% of the fully-diluted number of ordinary shares outstanding as of December 31 of the immediately preceding calendar year, or a lesser number as determined by the administrator. However, the maximum number of ordinary shares available for issuance as incentive stock options will be increased by the least of 4% of the fully-diluted number of ordinary shares outstanding on December 31 of the immediately preceding calendar year, 1,500,000 ADSs (or 75,000,000 ordinary shares after taking into account the 50-to-1 stock split on November 25, 2005) or a smaller number as determined by the administrator. In the year ended December 31, 2009, the number of shares reserved under the 1999 Stock Incentive Plan was not increased. Where an award agreement permits the exercise or purchase of the award for a specified period of time following the recipient's termination of service with us, or the recipient's disability or death, the award will terminate to the extent not exercised or purchased on the last day of the specified period or the last day of the original term of the award, whichever occurs first. As of December 31, 2016, options outstanding and exercisable under the 1999 Stock Incentive Plan were both 0. Our 1999 Stock Incentive Plan terminated on March 2, 2006, the date of the listing of our ordinary shares on the SEHK; provided that options granted under the plan remain outstanding in accordance with their terms..



*1999 Employee Stock Purchase Plan.* Our 1999 employee stock purchase plan (“1999 Purchase Plan”) was approved by our board of directors in October 1999, was approved by our shareholders prior to the consummation of our initial public offering in August 2000 and is intended to qualify as an “employee stock purchase plan” under Section 423 of the Internal Revenue Code and to provide our employees with an opportunity to purchase ordinary shares or ADSs through payroll deductions. In May 2005, our board of directors adopted certain amendments to the 1999 Purchase Plan and in October 2005 our board of directors adopted and approved an amendment and restatement of 1999 Purchase Plan to amend various administrative terms in anticipation of our listing on the SEHK in Hong Kong. We have reserved 50,000,000 ordinary shares for issuance under our 1999 Purchase Plan, subject to adjustment upon certain changes in our capitalization. The number of ordinary shares which shall be made available for sale under the 1999 Purchase Plan, any share options granted pursuant to our 2005 Share Option Plan and any other plan (but not including our 2005 Share Incentive Plan) will not exceed 10% of the number of ordinary shares to be issued and outstanding immediately following the listing of our ordinary shares on the SEHK. In no event may an option be granted under our 1999 Purchase Plan if such grant would result in the total aggregate number of ordinary shares subject to all then outstanding purchase rights granted by us pursuant to our 1999 Purchase Plan, any share option granted pursuant to our 2005 Share Option Plan or any other plan (but not including our 2005 Share Incentive Plan) to exceed 30% of the issued and outstanding ordinary shares from time to time. At the annual general meeting in June 2008, the shareholders approved, adopted and ratified an amendment to the 1999 Purchase Plan to increase the number of shares issuable pursuant to the 1999 Purchase Plan from 50,000,000 to 70,000,000 ordinary shares.

Our board of directors or a committee designated by our board of directors, referred to as the “plan administrator”, administers our 1999 Purchase Plan. All of our employees who are regularly employed for more than five months in any calendar year and work more than 20 hours per week are eligible to participate in our 1999 Purchase Plan, subject to a 10 day waiting period after hiring. Non-employee directors, consultants and employees subject to the rules or laws of a non-U.S. jurisdiction that prohibit or make impractical their participation in the plan will not be eligible to participate. Our 1999 Purchase Plan designates offer periods, purchase periods and exercise dates. Offer periods are periods of three months commencing in February, May, August and November. Purchase periods will generally be three month periods. Exercise dates are the last day of each purchase period. In the event of a corporate transaction, the plan administrator may elect to shorten the offer periods then in progress and set a new exercise date for the purchase of ordinary shares or ADSs.

On the first day of each offer period, a participating employee will be granted a purchase right. A purchase right is a form of option to be automatically exercised on the forthcoming exercise dates within the offer period during which authorized deductions are to be made from the pay of participants and credited to their accounts under our 1999 Purchase Plan. When the purchase right is exercised, the participant’s withheld salary is used to purchase the ordinary shares or ADSs. The price per share at which the ordinary shares or ADSs are to be purchased under our 1999 Purchase Plan during any purchase period will be expressed as a percentage not less than the lower of (a) 90% of the fair market value of the ordinary shares or ADSs on the date of grant of the purchase right (which is the commencement of the offer period) or (b) 90% of the fair market value of the ordinary shares or ADSs on the date the purchase right is exercised. Purchase rights may not be assigned, transferred, pledged or otherwise disposed of in any way by the participant, other than by will or the laws of descent and distribution.

Payroll deductions may range from 1% to 10% in whole percentage increments of a participant’s regular base pay. The maximum number of ordinary shares or ADSs that any employee may purchase under our 1999 Purchase Plan during a purchase period is 100,000 ordinary shares or 2,000 ADSs. In addition, Section 423 of the U.S. Internal Revenue Code imposes a \$25,000 limit on the maximum amount of ordinary shares or ADSs that may be purchased under a tax-qualified employee stock purchase plan during any calendar year. The \$25,000 limit is determined at the fair market value of the ordinary shares or ADSs at the time such option is granted for each calendar year in which such option is outstanding.

The plan administrator has the authority to amend or terminate our 1999 Purchase Plan. The plan administrator may terminate any offer period on any exercise date if the plan administrator determines that the termination of the offer period is in the best interests of our company and its shareholders.

*2009 Employee Stock Purchase Plan.* As approved at the Extraordinary General Meeting held on May 30, 2009, we adopted the 2009 Employee Stock Purchase Plan (“2009 Purchase Plan”) along with our delisting from SEHK in September 2009. The terms and provisions of 2009 Purchase Plan are generally the same as the 1999 Purchase Plan. The 2009 Purchase Plan will also have a term of 10 years, if not terminated earlier. A total of 25,000,000 ordinary shares were reserved for issuance under the 2009 Purchase Plan starting November 2009. As approved by the annual general meeting held on June 22, 2012, additional 15,000,000 ordinary shares were reserved for issuance under the 2009 Purchase Plan. From 2014 to 2016, 12,999,450 shares had been issued under the 2009 Purchase Plan.

*2005 Share Option Plan.* Our 2005 share option plan was adopted by our board of directors in August 2005, was approved by our shareholders in November 2005 and took effect on March 2, 2006 (“2005 Share Option Plan”). The 2005 Share Option Plan provides for the granting to employees of incentive stock options within the meaning of Section 422 of the Internal Revenue Code and the granting of nonstatutory stock options to our employees, directors and consultants. Initially, the maximum aggregate number of shares reserved for issuance pursuant to all options (including incentive stock options) under the 2005 Share Option Plan is 100,000,000 ordinary shares, or 2,000,000 ADSs after taking into account the 50-to-1 stock split on November 25, 2005 and such number of shares shall not, when added to the remaining number of ordinary shares available for the grant of options under any other plan or employee share purchase plan, be greater than 10% of the number of ordinary shares outstanding as of the date of adoption of the 2005 Share Option Plan. The maximum number of shares that may be issued upon exercise of all outstanding (and unexercised) options under the 2005 Share Option Plan and any other plan of ours and any purchase rights granted by us pursuant to any employee share repurchase plan must not, in aggregate, exceed 30% of the number of ordinary shares outstanding from time to time. Where an award agreement permits the exercise or purchase of the award for a specified period of time following the recipient’s termination of service with us, or the recipient’s disability or death, the award will terminate to the extent not exercised or purchased on the last day of the specified period or the last day of the original term of the award, whichever occurs first. As of December 31, 2016, 166,957,900 options were outstanding, of which 131,774,600 were exercisable under the 2005 Share Option Plan.

*2005 Share Incentive Plan.* Our 2005 share incentive plan was adopted by our board of directors in August 2005, was approved by our shareholders in November 2005 and took effect on March 2, 2006 (“2005 Share Incentive Plan”). The 2005 Share Incentive Plan provides for the granting to our employees, directors and consultants of restricted shares, cash dividend equivalent rights, restricted share units or stock appreciation rights or similar right with a fixed or variable price related to the fair market value of our ordinary shares and with an exercise or conversion privilege related to the passage of time, the occurrence of one or more events, or the satisfaction of performance criteria or other conditions. Initially, the maximum aggregate number of shares which may be issued pursuant the 2005 Share Incentive Plan is 75,000,000 ordinary shares or 1,500,000 ADSs after taking into account the 50-to-1 stock split on November 25, 2005. In addition, a right entitling a grantee to compensation measured by dividends paid with respect to ordinary shares shall be payable solely in cash and shall not be deemed to reduce the maximum aggregate number of shares which may be issued under our 2005 Share Incentive Plan. Where an award agreement permits the exercise or purchase of the award for a specified period of time following the recipient’s termination of service with us, or the recipient’s disability or death, the award will terminate to the extent not exercised or purchased on the last day of the specified period or the last day of the original term of the award, whichever occurs first. As of December 31, 2016, 38,441,950 shares were outstanding under the 2005 Share Incentive Plan.

*2015 Share Incentive Plan* Our 2015 Share Incentive Plan was adopted by our board of directors in May 2015, was approved by our shareholders in July 2015 and took effect on March 3, 2016 (“2015 Share Incentive Plan”). The 2015 Share Incentive Plan succeeded our 2005 Share Option Plan and our 2005 Share Incentive Plan. The 2015 Share Incentive Plan provides for the granting to employees of incentive stock options within the meaning of Section 422 of the Internal Revenue Code and the granting of nonstatutory stock options to our employees, directors and consultants. The 2015 Share Incentive Plan also provides for the granting to our employees, directors and consultants of restricted shares, cash dividend equivalent rights, restricted share units or stock appreciation rights or similar right with a fixed or variable price related to the fair market value of our ordinary shares and with an exercise or conversion privilege related to the passage of time, the occurrence of one or more events, or the satisfaction of performance criteria or other conditions. As of December 31, 2016, 60,375,900 shares were outstanding, of which 6,632,700 were exercisable under the 2015 Share Incentive Plan.

Initially, the maximum aggregate number of new shares reserved for issuance pursuant to all options and grants (including incentive stock options and restrictive stock units) under the 2015 Share Incentive Plan is 100,000,000 ordinary shares, or 2,000,000 ADSs, plus the remaining balance rolled into the 2015 Share Incentive plan from the 2005 Share Option Plan and 2005 Share Incentive Plan, respectively. The maximum number of stock options and restrictive stock units granted under the 2015 Share Incentive Plan for stock options and restrictive stock units shall not each exceed 125,000,000 ordinary shares (2,500,000 ADSs). In addition, a right entitling a grantee to compensation measured by dividends paid with respect to ordinary shares shall be payable solely in cash and shall not be deemed to reduce the maximum aggregate number of shares which may be issued under our 2005 Share Incentive Plan. Where an award agreement permits the exercise or purchase of the award for a specified period of time following the recipient’s termination of service with us, or the recipient’s disability or death, the award will terminate to the extent not exercised or purchased on the last day of the specified period or the last day of the original term of the award, whichever occurs first. As of December 31, 2016, 166,957,900 stock options were outstanding (reflecting 3,339,158 ADSs), of which 131,774,600 (reflecting 2,635,492 ADSs) were exercisable under the 2005 Share Option Plan. As of December 31, 2016, 38,441,950 shares (reflecting 768,839 ADSs) were outstanding under the 2005 Share Incentive Plan. As of December 31, 2016, 60,375,900 shares were outstanding (reflecting 1,207,518 ADSs), of which 6,632,700 (reflecting 132,654 ADSs) were exercisable under the 2015 Share Incentive Plan.

## **Board Practices**

### *Duties of Directors*

Under Cayman Islands law, our directors have a duty of loyalty to act honestly in good faith with a view to promoting our best interests. Our directors also have a duty of care to exercise the care, diligence and skills that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association and the class rights vested under our memorandum and articles of association in the holders of the shares.

### *Terms of Directors and Officers*

Our articles of association provide for not less than five, nor more than nine, directors, although the holders of a majority of our shares may increase or reduce such limits. Our articles of association provide for our board of directors to be divided into three classes, designated Class I, Class II and Class III, with each class consisting of an equal number of directors or as nearly equal in number as the then total number of directors permits. The directors of each class have been elected for terms of three years ending in consecutive years. At each annual general meeting, successors to the class of directors whose terms expire at that annual general meeting are elected for new three year terms. If the number of directors is changed, any increase or decrease is apportioned among the classes so as to maintain the number of directors in each class as nearly equal as possible and any additional directors of any class elected to fill a vacancy resulting from an increase in such class shall hold office for a term that shall coincide with the remaining term of that class, but in no case will a decrease in the number of directors shorten the term of any incumbent directors. The term of executive officers is determined by our board of directors. There are no provisions of Cayman Islands law which require the term of executive officers to be for a particular period.

Our board of directors has the power at any time and from time to time to appoint any person to be a director, either to fill a casual vacancy or as an additional to the existing directors provided that the appointment does not cause the number of directors to exceed any number fixed by or in accordance with the articles of association as a maximum number of directors. Any director so appointed shall hold office only until one next annual general meeting and is then eligible for re-election at that meeting.

Our shareholders may by ordinary resolution remove any directors before the expiration of his period of office notwithstanding anything in the articles of association or in any agreement we have entered into with such director (but without prejudice to any claim for damages under any such agreement).

There are currently no shareholding qualifications or age restrictions for directors.

#### *Committees of the Board of Directors*

We have an audit committee, a compensation committee and a nominating committee. Each of our audit committee members qualifies as an “independent” director for purposes of the rules and regulations of NASDAQ. The audit committee is established by the Board primarily for the purpose of overseeing our accounting and financial reporting processes and audits of our financial statements. The Committee's responsibilities include (1) the appointment, retention, compensation and oversight of the work of our independent auditors, and for review of its qualifications, and (2) review of our system of internal controls. The Committee also maintains procedures for the receipt, retention and treatment of complaints received by us regarding accounting, internal controls, or auditing matters and for the confidential, anonymous submission by our employees of concerns regarding accounting or auditing matters. The audit committee meets at least four times per year, and also meets separately with the representatives of management at least annually. The audit committee held four meetings in 2016. Currently, Messrs. Tan, Lin and Lenehan serve on the audit committee.

The compensation committee establishes remuneration levels for our officers, performs the functions that are provided under our employee benefit programs and administers our long-term incentive, compensation and equity plans including our 2005 Share Incentive Plan, 2005 Share Option Plan, 2009 Employee Stock Purchase Plan, and 2015 Share Incentive Plan. Currently, Messrs. Lin and Austin serve on the compensation committee, each of whom qualify as “independent” directors for purposes of the rules and regulations of NASDAQ.

The nominating committee assists our board of directors in selecting nominees for election to our board of directors and makes recommendations to our board of directors from time to time, or whenever it shall be called upon to do so, regarding nominees for our board of directors. Currently, Messrs. Austin and Kumar serve on the nominating committee.

#### *Compensation Committee Interlocks and Insider Participation*

No member of our compensation committee serves as a member of the board of directors or the compensation committee of any entity that has one or more executive officers serving as a member of our board of directors or our compensation committee.

#### **Employees**

As of December 31, 2016, we had 363 full-time employees, of which 202 are engineers. 25 of our employees were based in the United States, 335 in Asia, and 3 in Cayman Islands. Our employees are not represented by any collective bargaining agreements, and we have never experienced a work stoppage. We believe our employee relations are good and well-maintained.

#### **ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS**

##### **MAJOR SHAREHOLDERS**

The following table sets forth information known to us with respect to the beneficial ownership of our ordinary shares, as of February 28, 2017, by each shareholder known by us to own beneficially more than 5% of our ordinary shares based on SEC filings as of February 28, 2017.

Name of Beneficial Owner	Shares Beneficially Owned	
	Number	Percent
Grandeur Peak Global Advisors, LLC	159,212,000	12.31%
DNB Asset Management AS	131,220,450	10.15%
Directors and members of our administrative, supervisory or management bodies	119,744,200	9.26%
Renaissance Technologies LLC	101,665,000	7.86%
Lloyd I. Miller, III	75,735,550	5.86%

Based on SEC filings as of February 28, 2017, Grandeur Peak Global Advisors, LLC beneficially owned 159,212,000 of our ordinary shares or 12.31%, DNB Asset Management AS beneficially owned 131,220,450 of our ordinary shares or 10.15%, Directors and members of our administrative, supervisory or management bodies beneficially owned 119,744,200 of our ordinary shares or 9.26%, Renaissance Technologies LLC beneficially owned 101,665,000 of our ordinary shares or 7.86%, and Lloyd I. Miller, III beneficially owned 75,735,550 of our ordinary shares or 5.86%.

Based on SEC filings as of March 31, 2016, Grandeur Peak Global Advisors, LLC beneficially owned 159,212,000 of our ordinary shares or 12.38%, DNB Asset Management AS beneficially owned 131,220,450 of our ordinary shares or 10.20%, Directors and members of our administrative, supervisory or management bodies beneficially owned 114,953,950 of our ordinary shares or 8.94%, Renaissance Technologies LLC beneficially owned 99,230,000 of our ordinary shares or 7.71%, and Lloyd I. Miller, III beneficially owned 71,250,000 of our ordinary shares or 5.54%.

Based on SEC filings as of March 31, 2015, DNB Asset Management AS beneficially owned 133,070,900 of our ordinary shares or 10.04%, Directors and members of our administrative, supervisory or management bodies beneficially owned 104,670,500 of our ordinary shares or 7.90%, Renaissance Technologies LLC beneficially owned 99,010,000 of our ordinary shares or 7.47%, and Grandeur Peak Global Advisors, LLC beneficially owned 79,604,200 of our ordinary shares or 6.01%. Also, on November 25, 2014, Lone Star Value Management LLC filed a Schedule 13D with the Securities Exchange Commission declaring it had obtained a 5.6% stake in the Company, and, as of March 31, 2015, Lone Star Value Management LLC beneficially owned 85,105,000 of our ordinary shares or 6.42%.

None of the major shareholders listed above have differing voting rights with respect to our ordinary shares. We do not know of any arrangements the operation of which may at a subsequent date result in a change in control of us. To our knowledge, we are not directly or indirectly owned or controlled by another corporation, by a foreign government or any other natural or legal person.

#### RELATED PARTY TRANSACTIONS

There were no related party transactions for the financial periods covered in this Annual Report.

#### ITEM 8. FINANCIAL INFORMATION

##### CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION

###### Consolidated Financial Statements

Our financial statements set forth in the accompanying index to Consolidated Financial Statements included in this Annual Report following Part IV beginning on page F-1 are hereby incorporated in this Annual Report. Our Consolidated Financial Statements are filed as part of this Annual Report.

###### DIVIDEND POLICY

We have never declared or paid any cash dividends on our ordinary shares or other securities and do not anticipate paying cash dividends in the foreseeable future.

#### ITEM 9. THE OFFER AND LISTING

##### ADS SHARE PRICES AND RELATED MATTERS

Our ADSs are quoted and traded on the NASDAQ Global Select Market and the Cayman Islands Stock Exchange. Our ordinary shares are listed, but not traded, on the Cayman Islands Stock Exchange.

(a) Annual high and low market prices		
	High	Low
January 1, 2012 through December 31, 2012	\$5.65	\$2.90
January 1, 2013 through December 31, 2013	\$3.60	\$2.71
January 1, 2014 through December 31, 2014	\$3.89	\$1.90
January 1, 2015 through December 31, 2015	\$2.80	\$1.41
January 1, 2016 through December 31, 2016	\$2.07	\$1.27
(b) Quarterly high and low market prices		
First Quarter 2014	\$3.85	\$2.86
Second Quarter 2014	\$3.89	\$3.20
Third Quarter 2014	\$3.37	\$2.58
Fourth Quarter 2014	\$2.69	\$1.90
First Quarter 2015	\$2.62	\$2.31
Second Quarter 2015	\$2.75	\$2.20
Third Quarter 2015	\$2.80	\$2.17
Fourth Quarter 2015	\$2.33	\$1.41
First Quarter 2016	\$1.57	\$1.27
Second Quarter 2016	\$1.58	\$1.37
Third Quarter 2016	\$1.92	\$1.53
Fourth Quarter 2016	\$2.07	\$1.66
(c) Monthly high and low market prices		
October 2016	\$1.87	\$1.66
November 2016	\$2.07	\$1.77
December 2016	\$2.03	\$1.80
January 2017	\$2.74	\$1.89
February 2017	\$2.55	\$2.20

#### ITEM 10. ADDITIONAL INFORMATION

The following are summaries of material provisions of our memorandum and articles of association and the Companies Law (2011 Revision of the Cayman Islands (as amended, the "Companies Law")). The summary is qualified in its entirety by reference to our memorandum and articles of association (see Item 19-Exhibit 1).

##### Registered Office

The Company has been assigned registration number MC-72204 by the registrar of companies in the Cayman Islands. The registered office is located at the offices of Maples Corporate Services Limited, Ugland House, P.O. Box 309, South Church Street, Grand Cayman KY1-1104, Cayman Islands. The telephone number at that location is (345) 949-8066.

##### Objects and Purposes

Paragraph 3 of the memorandum of association provides that the objects and purposes of the Company are unrestricted and the Company may perform all corporate activities not prohibited by any law as provided by the Companies Law.

##### Directors

Article 122 of the articles of association of the Company provides that a director will not be disqualified by his office from contracting with the Company notwithstanding such director's interest and that such an interested director will not be liable to the Company for any profit realized through such contract or arrangement, provided, the interested director declares such interest at or prior to consideration of such contract or arrangement by the board. Article 129 provides that directors' compensation shall from time to time be determined by the Company in general meeting or by the board in accordance with the articles of association. Article 138 provides that the directors may exercise all the powers of the Company to borrow money and to mortgage or charge its undertaking, property and uncalled capital or any part thereof and to issue debentures, debenture stock and other securities whether outright or as security for any debt, liability or obligation of the Company or of any third party.

##### Ordinary Shares

*General.* The Company's articles of association authorize the issuance of 4,750,000,000 ordinary shares with a par value of US \$0.00002. All the outstanding ordinary shares are fully paid and nonassessable and accordingly no further capital may be called for by the Company from any holder of the ordinary shares outstanding. The outstanding ordinary shares are not entitled to any sinking fund or pre-emptive or redemption rights. Under Cayman Islands Law, non-residents may freely hold, vote and transfer ordinary shares in the same manner as Cayman Islands residents, subject to the provisions of the Companies Law and the articles of association. There is no exchange control legislation in the Cayman Islands or any laws or regulations which affect the payment of dividends to non-residents holders of the ordinary shares.

*Dividends.* The holders of our ordinary shares are entitled to receive the dividends that are declared and approved by the board of directors. Dividends may be paid only out of profits, which include net earnings and retained earnings undistributed in prior years, and out of share premium, a concept analogous to paid-in-surplus in the United States, subject to a statutory solvency test.



*Voting Rights.* Each ordinary share entitles the holder thereof to one vote on a show of hands and one vote in respect to each ordinary share held by that shareholder on a poll, on all matters upon which the ordinary shares are entitled to vote, including the election of directors. Voting at any meeting of shareholders is by show of hands unless a poll is demanded. A poll may be demanded by the chairman of the meeting or any shareholder present in person or by proxy, before or on the declaration of the result of the show of hands.

A quorum required for a meeting of shareholders consists of at least a number of shareholders present in person or by proxy and entitled to vote representing the holders of not less than a majority of our issued voting share capital. Shareholders' meetings are held annually and may be convened by the board of directors on its own initiative. Subject to the articles of association, advanced notice of at least ten days (but not more than sixty days) is required for the convening of shareholders' meetings.

Any ordinary resolution to be made by the shareholders requires the affirmative vote of a simple majority of the votes attaching to the ordinary shares and preference shares, if any, cast in a general meeting, while a special resolution requires the affirmative vote of two-thirds of the votes cast attaching to the ordinary shares and preference shares, if any. Holders of ordinary shares, which are currently the only shares carrying the right to vote at our general meetings, have the power, among other things, to elect directors, appoint auditors and make changes in the amount of our authorized share capital.

Material issues that require a special resolution of the shareholders under the Companies Law include resolutions to alter the memorandum of association with respect to any objects, powers or other matters specified therein, any alteration of the articles of association, any reduction of capital, any change of name, the appointment of an inspector for examining into the affairs of the company, requiring the company to be wound up by a court, any voluntary winding up, delegating to creditors the power of appointing liquidators, making binding arrangements between the company and its creditors, and sanctioning the transfer of the business or property of the company being wound up to another company whether established in the Cayman Islands or in any other jurisdiction.

*Liquidation.* If we are to be liquidated, the liquidator may divide among the shareholders in cash or in kind the whole or any part of our assets, in a manner proportionate to their shareholdings.

### **Preference Shares**

The articles of association authorize the issuance of 250,000,000 preference shares with a par value of \$0.00002 per share. Pursuant to our articles of association, the board of directors has the authority, without further action by the shareholders, to issue preference shares in one or more series. It also has the authority to allot, issue, grant options over, or otherwise dispose of, shares of the Company with or without preferred, deferred or other special rights or restrictions, whether in regard to dividend rights voting, return of capital or otherwise, any or all of which may be greater than the rights of the ordinary shares. The board of directors, without shareholder approval, can issue preference shares with voting, conversion or other rights that could harm the voting power and other rights of the holders of ordinary shares. Subject to the directors' duty of acting in our best interest, preference shares can be issued quickly with terms calculated to delay or prevent a change in control or make removal of management more difficult. Additionally, the issuance of preference shares may have the effect of decreasing the market price of the ordinary shares, and may harm the voting and other rights of the holders of ordinary shares.

### **Anti-takeover Effects of Provisions in Our Charter Documents**

Provisions in our charter documents could discourage potential acquisition proposals and could delay or prevent a change in control transaction that our shareholders favor. These provisions could have the effect of discouraging others from making tender offers for our shares. As a result, these provisions may prevent the market price of our ordinary shares from reflecting the effects of actual or rumored takeover attempts and may prevent shareholders from reselling their shares at or above the price at which they purchased their shares. These provisions may also prevent changes in our management that our shareholders may favor. Our charter documents do not permit shareholders to act by written consent, do not permit shareholders to call a general meeting and provide for a classified board of directors, which means shareholders can only elect, or remove, a limited number of our directors in any given year. Furthermore, as discussed above, our board of directors has the authority to issue up to 250,000,000 preference shares in one or more series. Our board of directors can fix the price, rights, preferences, privileges and restrictions of such preference shares without any further vote or action by our shareholders. The issuance of preference shares may delay or prevent a change in control transaction without further action by our shareholders or make removal of management more difficult.

### **Differences in Corporate Law**

The Companies Law of the Cayman Islands is modeled after that of England but does not follow recent United Kingdom statutory enactments and differs from laws applicable to United States corporations and their shareholders. The following paragraphs are a summary of the significant differences between the provisions of the Companies Law applicable to us and the laws applicable to companies incorporated in the United States and to their shareholders.

*Mergers and Similar Arrangements.* The Companies Law provides that a merger or consolidation may occur between any of the following: (a) one or more companies incorporated under the Companies Law and one or more companies incorporated under the laws of a jurisdiction outside the Cayman Islands, provided that the Cayman Islands company is the surviving entity; or (b) two or more companies incorporated under the Companies Law. For these purposes, (i) "merger" means the merging of two or more constituent companies and the vesting of their undertaking, property and liabilities in one of such companies as the surviving company and (ii) "consolidation" means the combination of two or more constituent companies into a consolidated company and the vesting of the undertaking, property and liabilities of such companies to the consolidated company. Such a merger or consolidation does not need court approval for a company limited by shares (but not segregated portfolio companies).

A merger or consolidation will involve, amongst other things, the directors of each company participating in a merger or consolidation approving a written plan of merger or consolidation on behalf of that company which complies with the requirements of the Companies Law. The written plan of merger or consolidation approved by the directors must generally be authorised by resolution of the shareholders of each company participating in the merger or consolidation, subject to and in accordance with the Companies Law. The consent of each holder of a fixed or floating security interest of a company participating in a proposed merger or consolidation should also be obtained, although the courts of the Cayman Islands have a discretion to waive such requirement upon such terms as to the security to be issued by the consolidated or surviving company as the court considers reasonable.

A dissenting member of a Cayman Islands company proposing to participate in a merger or consolidation has a limited entitlement provide written objection to the proposed action and to receive payment of the fair value of his shares in accordance with the provisions of the Companies Law.

If a merger or consolidation is effected in accordance with the Companies Law:

- the rights, the property of every description and the business, undertaking, goodwill, benefits, immunities and privileges of each of the constituent companies, shall immediately vest in the surviving or consolidated company;
- subject to any specific arrangements entered into by the relevant parties, the surviving or consolidated company shall be liable for and subject, in the same manner as the constituent companies, to all mortgages, charges or security interests, and all contracts, obligations, claims, debts, and liabilities of each of the constituent companies;
- an existing claim, cause or proceeding, whether civil (including arbitration) or criminal pending at the time of the merger or consolidation by or against a constituent company, shall not be abated or discontinued by the merger or consolidation but shall be continued by or against the surviving or consolidated company; and
- a conviction, judgment, ruling, order or claim, due or to become due, against a constituent company, shall not be released or impaired by the merger or consolidation, but shall apply to the surviving or consolidated company instead of to the constituent company.

Cayman Islands law also provides statutory provisions which facilitate the reconstruction and amalgamation of companies, provided that the arrangement in question is approved by a majority in number of each class of shareholders and creditors with whom the arrangement is to be made, and who must in addition represent three-fourths in value of each class of shareholders or creditors, as the case may be, that are present and voting either in person or by proxy at a meeting or meetings convened for that purpose. The convening of the meetings and subsequently the arrangement must be sanctioned by the Grand Court of the Cayman Islands. While a dissenting shareholder would have the right to express to the court the view that the transaction ought not to be approved, the court can be expected to approve the arrangement if it satisfies itself that:

- the parties have complied with the statutory provisions regarding majority vote;
- the shareholders have been fairly represented at the meeting in question; and
- the arrangement is one that a businessman would reasonably approve.

When a take-over offer is made and accepted by holders of 90% in value of the shares within four months, the offer or may, within a two-month period require the holders of the remaining shares to transfer these shares on the terms of the offer. An objection can be made to the Grand Court of the Cayman Islands but this is unlikely to succeed unless there is evidence of fraud, bad faith or collusion.

If the arrangement and reconstruction is approved, the dissenting shareholder would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of United States corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

*Shareholders' Suits.* In principle, we will normally be the proper plaintiff in respect of wrongs done to the Company and a derivative action may not be brought by a minority shareholder. However, exceptions to the foregoing principle may apply in circumstances in which:

- a company is acting or proposing to act illegally or outside of its powers;
- the act complained of, although not outside of its powers, could be affected only if authorized by more than a simple majority vote;
- the individual rights of the plaintiff shareholders have been infringed or are about to be infringed; or
- those who control the company are perpetrating a "fraud on the minority."



## **Indemnification**

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent that a provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Our articles of association provide for indemnification of officers and directors for losses, damages, costs and expenses incurred in their capacities as such, except if they acted in a willfully negligent manner or defaulted in any action against them.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to our directors, officers or persons controlling us pursuant to these provisions, we have been informed that, in the opinion of the Securities and Exchange Commission, this indemnification is against public policy as expressed in the Securities Act and therefore is unenforceable.

## **Enforceability of Civil Liabilities**

We are a Cayman Islands company. We incorporated in the Cayman Islands because of the following benefits associated with being a Cayman Islands company:

- political and economic stability;
- an effective judicial system;
- unlike some jurisdictions which impose taxes on worldwide income, no taxation of companies based upon profits, income, gains or appreciation;
- the absence of exchange control or currency restrictions; and
- the availability of professional and support services.

However, the Cayman Islands has a less developed body of securities laws than the United States and provides less protection for investors. Under Cayman Islands law, our directors have a duty of loyalty to act honestly and in good faith with a view to promoting our best interests. Our directors also have a duty of care to exercise the care, diligence and skills that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association and the class rights vested under our memorandum and articles of association in the holders of the shares. The remedies which may be pursued if our directors do not comply with their duties to us are well settled matters of Cayman Islands law.

A substantial majority of our assets are located outside the United States. In addition, a majority of our directors and officers are nationals and/or residents of countries other than the United States, and all or a substantial portion of our assets and the assets of our directors and officers are located outside the United States. As a result, it may be difficult to effect service of process within the United States upon us or our directors and officers or to enforce against us or against them judgments obtained in United States courts, including judgments predicated upon the civil liability provisions of the securities laws of the United States or any state thereof. Nevertheless, the courts of the Cayman Islands would be competent to hear original actions brought by us against our officers and directors predicated upon alleged breaches of duties to us.

Maples and Calder, our counsel as to Cayman Islands law, has advised us that there is uncertainty regarding whether the courts of the Cayman Islands would (1) recognize or enforce judgments of United States courts obtained against us or our officers and directors predicated upon the civil liability provisions of the securities laws of the United States or any state thereof or (2) be competent to hear original actions brought in their jurisdiction against us or our officers and directors predicated upon the securities laws of the United States or any state thereof.

There is no statutory enforcement in the Cayman Islands of judgments obtained in the United States. Instead, such a judgment must be enforced by action at common law. Maples and Calder have advised us that a final and conclusive judgment in a federal or state court of the United States under which a sum of money is payable, other than a sum payable in respect of taxes, fines, penalties or similar charges, may be subject to enforcement proceedings as a debt in the Courts of the Cayman Islands under the common law doctrine of obligation.

## **Material Contracts**

We have not entered into any material contracts other than contracts entered into in the ordinary course of business.

## **Exchange Control**

Our articles of association authorize us to issue an aggregate of 4,750,000,000 ordinary shares with a par value of \$0.00002 per share. Of those 4,750,000,000 authorized ordinary shares, 1,669,036,600 shares were issued and 1,279,124,900 shares were outstanding as of December 31, 2016, all of which are fully paid or credited as fully paid. We may not call for any further capital from any holder of ordinary shares outstanding. Under Cayman Islands law, non-residents of the Cayman Islands may freely hold, vote and transfer ordinary shares in the same manner as Cayman Islands residents, subject to the provisions of the Companies Law and our articles of association. There is no exchange control legislation in the Cayman Islands or any laws or regulations which affect the payment of dividends to non-resident holders of ordinary shares.

## TAXATION

### Cayman Islands Taxation

The Cayman Islands currently levy no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to us levied by the Government of the Cayman Islands except for stamp duties that may be applicable on instruments executed in, or after execution brought within, the jurisdiction of the Cayman Islands. There are no exchange control regulations or currency restrictions in the Cayman Islands.

No stamp duties are payable on the issue or transfer of shares. An agreement to transfer shares may be subject to stamp duty if the agreement is executed in the Cayman Islands or, if executed outside the Cayman Islands, subsequently brought into the Cayman Islands. The Stamp Duty Law (2007 Revision) does not provide who is liable to pay stamp duty on any document but, in practice, the person who seeks to rely on the document in any civil court proceedings will be required to pay stamp duty in order to have the document admitted in evidence.

### United States Federal Income Taxation

The following discussion addresses the material United States federal income tax consequences of the ownership and disposition of ordinary shares or ADSs held as a capital asset by a "U.S. Investor" (as defined below). This summary does not provide a complete analysis of all potential tax consequences. This summary is based on the Internal Revenue Code of 1986, as amended (the "Code"), final, temporary and proposed Treasury Regulations thereunder, and administrative and judicial interpretations thereof, all as in effect as of the date hereof, and all of which are subject to change at any time (possibly on a retroactive basis) by legislative, judicial or administrative action, and to differing interpretations. There can be no assurance that the Internal Revenue Service (the "IRS") will not take a contrary view. This summary does not discuss state, local or foreign tax consequences of the ownership and disposition of ordinary shares or ADSs.

This summary is directed solely to U.S. Investors that hold ordinary shares or ADSs as capital assets within the meaning of Section 1221 of the Code, which generally means as property held for investment. For purposes of this discussion, a "U.S. Investor" means a beneficial owner of ordinary shares or ADSs who is any of the following:

- a citizen or resident of the United States or someone treated as a U.S. citizen or resident for U.S. federal income tax purposes;
- a corporation or other entity taxable as a corporation for U.S. federal income tax purposes created or organized in or under the laws of the United States or any political subdivision thereof, including the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation regardless of its source;
- a trust that is subject to the primary supervision of a court within the United States and one or more U.S. persons have the authority to control all of its substantial decisions;
- a trust in existence on August 20, 1996, that has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person; or
- a person that is otherwise subject to U.S. federal income taxation on its net income.

If a partnership (including for this purpose any entity treated as a partnership for U.S. federal income tax purposes) is a beneficial owner of ordinary shares or ADSs, the U.S. federal income tax consequences to a partner in the partnership will generally depend on the status of the partner and the activities of the partnership. A holder of ordinary shares or ADSs that is a partnership and partners in such partnership should consult their individual tax advisors about the U.S. federal income tax consequences of holding or disposing of the ordinary shares or ADSs.

This summary does not address the United States federal income tax treatment of investors having a special legal status, including without limitation the following types of investors, who may be subject to tax rules that differ significantly from those summarized below:

- life insurance companies;
- tax-exempt investors;
- banks and financial institutions;
- dealers in securities or foreign currencies;
- traders in securities that elect to use a mark-to-market method of accounting for their securities holdings;

- persons liable for alternative minimum tax;
- U.S. investors who actually or constructively hold 10% or more of our voting shares or ADSs;
- investors who hold our ordinary shares or ADSs as part of straddles, hedging or integrated or conversion transactions; or
- persons whose “functional currency” is not the U.S. dollar.

This summary is not a comprehensive description of all of the tax considerations that may be relevant with respect to your ownership of ordinary shares or ADSs. You are advised to consult your own tax adviser with respect to your particular circumstances and with respect to the effects of federal, state, local or foreign tax laws to which you may be subject. The United States does not have an income tax treaty with the Cayman Islands.

As relates to the ADSs, this discussion is based in part upon the representations of the depositary and the assumption that each obligation in the deposit agreement and any related agreement will be performed in accordance to its terms.

Generally, a holder of ADSs will be treated as the owner of the underlying ordinary shares represented by those ADSs for U.S. federal income tax purposes. Accordingly, no gain or loss will be recognized if the holder exchanges ADSs for the underlying ordinary shares represented by those ADSs. The holder's adjusted tax basis in the ordinary shares will be the same as the adjusted tax basis of the ADSs surrendered in exchange therefor, and the holding period for the ordinary shares will include the holding period for the surrendered ADSs.

*Dividends and Other Distribution on Ordinary Shares or ADSs.* Subject to the discussion in “Passive Foreign Investment Company Status” below, in the event that a U.S. Investor receives a distribution on the ordinary shares or ADSs, the U.S. Investor will be required to include the distribution in gross income as a taxable dividend on the date of receipt by the depositary, in the case of ADSs, or by the U.S. Investor, in the case of ordinary shares, but only to the extent that a distribution is paid from our current or accumulated earnings and profits as determined under United States federal income tax principles. Dividends paid by us will not be eligible for the corporate dividends received deduction. For taxable years beginning before January 1, 2011, “qualified dividend income” paid to a non-corporate U.S. Investor will be subject to tax at the rates applicable to long-term capital gains (which are currently taxed at the maximum rate of 20%) if (1) our ordinary shares or ADSs are readily tradable on an established securities market in the United States, (2) we are not a passive foreign investment company (as discussed below) for either our taxable year in which the dividend was paid or the preceding taxable year and (3) certain holding period requirements must be met. It is expected that our ADSs will satisfy the “readily tradable” requirement as a result of being traded on the NASDAQ Global Select Market. However, any U.S. Investor that exchanges its ADSs for ordinary shares, or that holds only ordinary shares, may not be eligible for the reduced rate of taxation on dividends if the ordinary shares are not readily tradable on an established securities market in the United States. In order for dividends to constitute “qualified dividend income,” a U.S. Investor generally must have held the ADSs for more than 60 days during the 121-day period beginning 60 days before the ex-dividend date; however, because the holding period rules are intricate and because an owner's holding period is reduced for periods during which the risk of loss is diminished, U.S. Investors should consult their own advisors concerning the calculation of their holding periods. Moreover, a dividend will not be treated as a qualified dividend income to the extent that the taxpayer is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property. U.S. Investors should consult their own tax advisers regarding the availability of the lower rate for dividends paid with respect to our ADSs or ordinary shares.

The Company has the right to pay dividends in any currency. If dividends are paid in a currency other than the U.S. dollar, the dividends will be included in a U.S. Investor's income as a U.S. dollar amount based on the exchange rate in effect on the date that the U.S. Investor receives the dividend, regardless of whether the payment is in fact converted into U.S. dollars. If the U.S. Investor does not receive U.S. dollars on the date the dividend is distributed, the U.S. Investor will be required to include either gain or loss in income when the U.S. Investor later exchanges the foreign currency for U.S. dollars. The gain or loss will be equal to the difference between the U.S. dollar value of the amount that the U.S. Investor includes in income when the dividend is received and the amount that the U.S. Investor receives on the exchange of the foreign currency for U.S. dollars. The gain or loss generally will be ordinary income or loss from U.S. sources. If we distribute as a dividend non-cash property, the U.S. Investor will generally include in income an amount equal to the U.S. dollar equivalent of the fair market value of the property on the date that it is distributed.

Dividends will constitute foreign source income for foreign tax credit limitation purposes. The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. Under current law, for taxable years beginning after December 31, 2006, dividends distributed by us with respect to ordinary shares or ADSs would generally constitute “passive category income” but could, in the case of certain U.S. Investors, constitute “general category income.” Special rules apply to individuals whose foreign source income during the taxable year consists entirely of “qualified passive income” and whose creditable foreign taxes paid or accrued during the taxable year do not exceed \$300 (\$600 in the case of a joint return). Further, in particular circumstances, a U.S. Investor that (i) has held the ordinary shares or ADSs for less than a specified minimum period during which it is not protected from risk of loss, (ii) is obligated to make payments related to the dividends, or (iii) holds the ordinary shares or ADSs in arrangements in which the U.S. Investor's expected economic profit, after non-U.S. taxes, is insubstantial, will not be allowed a foreign tax credit for foreign taxes imposed on dividends paid on the ordinary shares or ADSs.

The U.S. Treasury has expressed concerns that parties to whom ADSs are pre-released may be taking actions that are inconsistent with the claiming of foreign tax credits by U.S. Investors of ADSs. Such actions would also be inconsistent with the claiming of the preferential tax rates applicable to qualified dividend income, as defined above. Accordingly, the creditability of foreign withholding taxes and the availability of such preferential tax rates could be affected by future actions that may be taken by the U.S. Treasury or parties to whom ADSs are pre-released.

Distributions in excess of our current and accumulated earnings and profits will be treated as a nontaxable return of capital to the extent of the U.S. Investor's basis in the ordinary shares or ADSs and thereafter as gain from the sale or exchange of a capital asset. We do not generally intend to calculate our earnings and profits under U.S. federal income tax principles. Therefore a U.S. Investor should expect that a distribution will generally be treated as a dividend even if that distribution would otherwise be treated as a nontaxable return of capital or as capital gain under the rules described above.

Distributions to a U.S. Investor of new ordinary shares or ADSs or rights to subscribe for new ordinary shares or ADSs that are received as part of a pro rata distribution to all our shareholders will not be subject to U.S. federal income tax. The adjusted tax basis of the new ordinary shares or ADSs or rights so received will be determined by allocating the U.S. investor's adjusted tax basis in the old ordinary shares or ADSs between the old ordinary shares or ADSs and the new ordinary shares or ADSs or rights received, based on their relative fair market values on the date of distribution. However, the adjusted tax basis of the new ordinary shares or ADSs or rights will be zero if the fair market value of the new rights is less than 15% of the fair market value of the old ordinary shares or ADSs at the time of distribution and the U.S. Investor does not make an election to determine the adjusted tax basis of the rights by allocation as described above. A U.S. Investor's holding period in the new ordinary shares or ADSs or rights will generally include the holding period of the old ordinary shares or ADSs on which the distribution was made.

*Dispositions of ordinary shares or ADSs.* Subject to the discussion in "Passive Foreign Investment Company Status" below, gain or loss realized by a U.S. Investor on the sale or other disposition of the ordinary shares or ADSs will be subject to United States federal income tax as capital gain or loss in an amount equal to the difference between the amount realized on the disposition and that U.S. Investor's basis in the ordinary shares or ADSs. The capital gain or loss will be long-term capital gain or loss if the U.S. Investor has held the ordinary shares or ADSs for more than one year at the time of the sale or exchange. A non-corporate U.S. investor will be eligible for reduced rates of taxation (currently, at a maximum rate of 20% for sales occurring in taxable years beginning before January 1, 2011,) on long-term capital gain. The deductibility of capital losses is subject to limitations. Any gain or loss recognized by a U.S. Investor will generally be treated as U.S. source income or loss for U.S. foreign tax credit purposes.

U.S. Investors should consult their own tax advisor regarding the U.S. federal income tax consequences if the U.S. Investor receives currency other than U.S. dollars upon the disposition of ordinary shares or ADSs.

*Passive Foreign Investment Company Status.* We believe that we are not a passive foreign investment company and do not expect to become a passive foreign investment company in the future. We will be classified as a passive foreign investment company if for a taxable year, after the application of "look through" rules, either (a) 75% or more of the gross income of the company in a taxable year is passive income, or (b) the average percentage of assets by value of the company in a taxable year that produce or are held for the production of passive income (which includes cash) is at least 50%, the income or assets test. Whether or not we are a passive foreign investment company will be determined annually based upon the composition of our income and assets including goodwill, from time to time. In determining that we are not a passive foreign investment company, we are relying on the current valuation of our assets, including goodwill. In calculating goodwill, we have valued our total assets based on our total market value determined using the then market price of our ordinary shares and ADSs and have made a number of assumptions regarding the amount of this value allocable to goodwill. Because the determination of goodwill will be based on the price of our ordinary shares and ADSs, it is subject to change. We believe our valuation approach is reasonable. However, it is possible that the Internal Revenue Service will challenge the valuation of our goodwill, which may result in our being classified as a passive foreign investment company. In addition, the composition of our income and assets will be affected by how we spend the cash we have raised, which is a passive asset for purposes of the passive foreign investment company asset test discussed above. We intend to use the cash we have raised in the past and conduct our business activities in an effort to reduce the risk of our classification as a passive foreign investment company. Because the passive foreign investment company determination is made at the end of each taxable year, we cannot determine in advance whether we will be considered a passive foreign investment company for any future taxable year. If we determine that we have become a passive foreign investment company, we will notify the Bank of New York and all U.S. investors who have been record holders of our ordinary shares or ADSs during any period in which we determine that we are a passive foreign investment company, within 60 days of the end of our taxable year for which we make such determination. If we are a passive foreign investment company for any year during which a U.S. Investor holds ordinary shares or ADSs, we generally will continue to be treated as a passive foreign investment company for all succeeding years during which the U.S. Investor holds ordinary shares or ADSs.

Special U.S. tax rules apply to U.S. Investors of interests in a passive foreign investment company. Subject to the discussion of the market-to-market election and qualified electing fund election below, if we were a passive foreign investment company for any taxable year during which a U.S. Investor held ordinary shares or ADSs, the U.S. Investor would be subject to special tax rules regardless of whether we meet the income or assets test for any other year with respect to:

- any "excess distribution" by us to the U.S. Investor, which means any distributions received by the U.S. Investor on the ordinary shares or ADSs in a taxable year that are greater than 125% of the average annual distributions received by the U.S. Investor in the three preceding taxable years, or, if shorter, the U.S. Investor's holding period for the ordinary shares or ADSs; and
- any gain realized on the sale or other disposition, including a pledge, of ordinary shares or ADSs.

Under these special tax rules:

- the excess distribution or gain would be allocated ratably over the U.S. Investor's holding period for the ordinary shares or ADSs;
- the amount allocated to the current taxable year and any taxable year prior to the first taxable year in which we are a passive foreign investment company would be treated as ordinary income in the current year;
- the amount allocated to each of the other years would be taxed as ordinary income at the highest tax rate in effect for that year; and
- the interest charge applicable to underpayments of tax would be imposed with respect to the resulting tax attributable to each prior year in which we were a passive foreign investment company to recover the deemed benefit from the deferred payment of the tax attributable to each prior year.

In addition, dividends that a U.S. Investor receives from us will not be eligible for the special tax rates applicable to "qualified dividend income" (see "-- United States Federal Income Taxation --- Dividends") if we are a passive foreign investment company either in the taxable year of the distribution or the preceding taxable year, but will instead be taxable at rates applicable to ordinary income.

If we are a passive foreign investment company in any year, a U.S. Investor would be required to file an annual return on Internal Revenue Service Form 8621 regarding distributions received with respect to the ordinary shares or ADSs and any gain realized on the disposition of the ordinary shares or ADSs.

A U.S. Investor in a passive foreign investment company is allowed to make a mark-to-market election with respect to the stock of the passive foreign investment company, provided that the stock of the passive foreign investment company is "marketable" within the meaning of the Code. The ordinary shares or ADSs will be "marketable" as long as they remain listed on the NASDAQ Global Select Market and are "regularly traded." The ordinary shares or ADSs will be considered "regularly traded" for any calendar year during which the ordinary shares or ADSs are traded, other than in de minimis quantities, on at least fifteen days during each calendar quarter. If the election is made, a U.S. Investor would be required to mark the ordinary shares or ADSs to market each taxable year and recognize ordinary income for any increase in market value for that taxable year and would be allowed to recognize an ordinary loss for any decrease in that market value to the extent that prior gains exceed prior losses. The adjusted basis in the ordinary shares or ADSs would be adjusted to reflect that gain or loss. The mark-to-market election will be effective for the taxable year for which the election is made and all subsequent taxable years, unless the ordinary shares cease to be marketable or the Internal Revenue Service consents to the revocation of the election.

Alternatively, for each year we meet the income or assets test, a U.S. Investor can make an election to include in income annually its pro rata share of our earnings and net capital gains. This election is referred to as a qualified electing fund election. To make a qualified electing fund election, a U.S. Investor will need to have an annual information statement from us documenting the earnings and capital gain for the year. If we were to become a passive foreign investment company, we would furnish the passive foreign investment company annual information statement to any shareholder or former shareholder who requested it. In general, a U.S. Investor must make a qualified electing fund election on or before the due date for filing its income tax return for the first year to which the qualified electing fund election will apply. U.S. Investors are permitted to make retroactive elections in particular circumstances, including if the U.S. Investor had a reasonable belief that the foreign corporation was not a passive foreign investment company and filed a protective election. As discussed above, we will notify investors if we determine that we have become a passive foreign investment company. This notice will provide U.S. Investors on a calendar tax year with sufficient time to make the qualified electing fund election. U.S. Investors (in particular those with a tax year other than the calendar year) should consult their own tax advisors as to the consequences of making a protective qualified electing fund election or other consequences of the qualified electing fund election.

If we are a passive foreign investment company in any year, U.S. Investors should consult with their tax advisers regarding whether to make a mark-to-market or qualified electing fund election.

*Information Reporting and Backup Withholding.* In general, information reporting requirements will apply to dividends in respect of our ordinary shares or ADSs or the proceeds received on the sale, exchange or redemption of our ordinary shares or ADSs paid within the United States (and, in certain cases, outside the United States) to U.S. Investors other than certain exempt recipients, such as corporations, and a backup withholding tax (currently at a rate of 28%) may apply to such amounts if the U.S. Investor fails to provide an accurate taxpayer identification number or to report interest and dividends required to be shown on its U.S. federal income tax returns. U.S. Investors who are required to establish their exempt status generally must provide such certification on IRS Form W-9.

Backup withholding is not an additional tax. Amounts withheld as backup withholding from a payment to a U.S. Investor may be allowed as a credit against the U.S. Investor's U.S. federal income tax liability and the U.S. Investor may obtain a refund of any excess amounts withheld by filing the appropriate claim for refund with the IRS and furnishing any required information in a timely manner.

## DOCUMENTS ON DISPLAY

We file annual reports on Form 20-F and furnish current reports on Form 6-K with the SEC. You may read and copy this information at the SEC's Public Reference Room at Judiciary Plaza, 100 F Street N.E., Washington, D.C. 20549, and at the regional offices of the SEC located at 3 World Financial Center, Suite 400, New York, New York 10281 and 175 W. Jackson Boulevard, Suite 900, Chicago, Illinois 60604. You can also request copies of the documents, upon payment of a duplicating fee, by writing to the Public Reference Section of the SEC. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the Public Reference Room. Certain of our SEC filings are also available to the public from the SEC's website at <http://www.sec.gov>.

## ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the risk of loss related to adverse changes in market prices, including interest rates and foreign exchange rates, of financial instruments. In the normal course of business, our financial position is routinely subject to a variety of risks, including market risk associated with interest rate movements and currency rate movements on non-U.S. dollar denominated assets and liabilities, as well as collectability of accounts receivable.

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

### *Interest Rate Risk*

Our major market risk exposure is changing interest rates. Our exposure to market risk for changes in interest rates relates primarily to our investments in time deposits.

We generally maintain an investment portfolio consisting mainly of fixed income securities, including time deposits. These securities are subject to interest rate risk and will fall in value if market interest rates increase. We do not believe that a 10.0% change in interest rates would have a significant impact on the fair value of our investment portfolio. There was no exposure to market risk at December 31, 2016. We have not purchased and do not currently hold any derivative financial instruments for hedging or trading purposes.

The table below provides information about our financial instruments whose maturity dates are greater than three months as of December 31, 2016.

	2017	2018	2019	2020	2021	Thereafter	Total	Fair Value
	<i>(in thousands)</i>							
<b>Time Deposit:</b>								
Fixed rate (US\$)	\$ 8,636	\$ 28	\$ -	\$ -	\$ -	\$ -	\$ 8,664	\$ 8,664

### *Foreign currency risk*

Fluctuations in exchange rates may adversely affect our financial results. The functional currency for each of our foreign subsidiaries is the local currency. As a result, certain of our assets and liabilities, including certain bank accounts, accounts receivable, restricted assets, short-term investments and accounts payable, exist in non-US dollar-denominated currencies, which are sensitive to foreign currency exchange rate fluctuations. If exchange rates were to change immediately and uniformly from the levels at December 31, 2016, the fair value of such assets and liabilities would change by an immaterial amount beyond the change reflected by the exchange rates. As of December 31, 2016, we held approximately \$9.1 million in certificates of deposits and bank demand accounts denominated in foreign currencies.

We have not engaged in hedging techniques to mitigate foreign currency exposures and may experience economic losses as a result of foreign currency exchange rate fluctuations. We will monitor currency exchange fluctuations periodically. For the year ended December 31, 2016, we experienced a net foreign exchange gain of approximately \$63,000 due to foreign currency exchange fluctuations, which are reflected in our results of operations.

## ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

### A. Debt Securities

Not applicable.

### B. Warrants and Rights

Not applicable.

### C. Other Securities

Not applicable.

#### D. American Depositary Shares

Our American Depositary Receipt (“ADR”) facility is maintained by the Bank of New York Mellon (the “Depository”). A copy of the form of Deposit Agreement (the “Deposit Agreement”) between us, the Depository, and the owners and beneficial owners of ADSs was filed as Exhibit 1 to our Registration Statement on Form S-6 filed with the SEC on November 7, 2005. The Hong Kong and Shanghai Banking Corporation (the “Custodian”) acts as an agent of the Depository for the purposes of the Deposit Agreement.

#### **Fees and charges payable by our ADS holders**

Under the Deposit Agreement, the Depository collects fees for the delivery and surrender of ADSs directly from investors depositing ordinary shares or surrendering ADSs for the purpose of withdrawal or from intermediaries acting for them. The depository collects fees for making distributions to investors by deducting those fees from the amounts distributed or by selling a portion of distributable property to pay the fees. The depository may collect its annual fee for depository services by deductions from cash distributions, directly billing investors or charging the book-entry system accounts of participants acting for them. The charges of our Depository payable by our ADS holders are as follows, pursuant to the Deposit Agreement:

#### **ADS holders must pay:**

\$5.00 or less per 100 ADSs

\$5.00 or less per 100 ADSs

\$0.02 or less per ADS

A fee equivalent to the fee for the execution and delivery of ADSs referred to above which would have been charged as a result of the deposit of such securities but which securities are instead distributed by the Depository to registered ADS holders

\$0.02 or less per ADS per calendar year (to the extent that the depository has not collected a cash distribution fee of US\$0.02 per ADS during that year)

Registration or transfer fees, if applicable

Expenses of the depository, if applicable

Taxes and other governmental charges the Depository or the Custodian have to pay on any ADS or ordinary share underlying an ADS, for example, stock transfer taxes, stamp duty or withholding taxes

Any charges incurred by the Depository or its agents for servicing the deposited securities

#### **For:**

- Each delivery or issuance of ADSs, including deliveries or issuances resulting from a distribution of shares or rights or other property
- Each surrender or cancellation of ADSs for the purpose of withdrawal, including if the deposit agreement terminates
- Any cash distribution to ADS registered holders
- Each distribution of securities, other than ordinary shares or ADSs, to holders of deposited securities which are distributed by the Depository to ADS registered
- Depository services
- Transfer and registration of shares on the share register of our transfer agent to or from the name of the Depository or its agent when an ADS holder deposits or withdraws shares
- Cable, telex and facsimile transmissions as are expressly provided in the deposit agreement
- Converting foreign currency to U.S. dollars
- As necessary
- As necessary

## **Fees and payments made by the Depositary to us**

The Depositary has waived certain of its standard out-of-pocket administrative, maintenance, shareholder services and secondary market support services fees and expenses for providing services to registered ADS holders and us (excluding those fees and expenses set forth in the table above). These waived fees and expenses include, without limitation, the Depositary's annual administration charges and fees, custody fees, issuance of dividend checks and replacements, if necessary, preparation and filing of U.S. tax information returns, stationery, postage, notification mailing, photocopying, facsimile and telephone calls, and certain investor relationship programs and investor relations promotional activities. We are responsible for paying for postage and envelopes for mailing annual and interim financial reports and all non-standard out-of-pocket administration and maintenance expenses of the Depositary, including any and all reasonable legal fees and disbursements.

## **PART II**

### **ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

There are no defaults, dividend arrearages or delinquencies that are required to be disclosed.

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

#### **RIGHTS OF SECURITY HOLDERS**

Effective March 2, 2006, upon the listing of our ordinary shares on the Stock Exchange of Hong Kong ("SEHK"), certain amendments to our Memorandum and Articles of Association became effective, as is described in the report on Form 6-K filed on March 1, 2006. A summary of material provisions of our Memorandum and Articles of Association is included in Item 10 above.

#### **USE OF PROCEEDS**

As of December 31, 2016, the net proceeds from our initial public offering in August 2000, and our public offering in November 2001, were primarily used for general working capital and investment in interest income producing financial instruments. None of the net proceeds from our initial public offering were paid, directly or indirectly, to any of our directors, officers or general partners or any of their associates, or to any person owning ten percent or more of any class of our equity securities, or any of our affiliates.

### **ITEM 15. CONTROLS AND PROCEDURES**

#### Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed pursuant to the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. In addition, the design of any control system is based in part upon certain assumptions about the likelihood of future events. Our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives.

As of December 31, 2016, we carried out an evaluation, under the supervision and with the participation of the management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on the foregoing, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

#### Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the company. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Our company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of our company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of our company are being made only in accordance with authorizations of management and directors of our company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our company's assets that could have a material effect on the financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. Management conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in Internal Control—Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, management concluded that our company's internal control over financial reporting was effective as of December 31, 2016. This Annual Report includes an attestation report of our independent registered public accounting firm regarding internal control over financial reporting.



Changes in Internal Control over Financial Reporting

There has been no change in our internal control over financial reporting that occurred during our fiscal year 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Attestation Report of The Independent Registered Public Accounting Firm

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and the Shareholders of O<sub>2</sub>Micro International Limited:

We have audited the internal control over financial reporting of O<sub>2</sub>Micro International Limited and subsidiaries (the “Company”) as of December 31, 2016, based on criteria established in *Internal Control - Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management’s Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit.

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

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

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

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the criteria established in *Internal Control - Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2016, of the Company and our report dated March 31, 2017 expressed an unqualified opinion on those financial statements.

/s/ Deloitte & Touche  
Taipei, Taiwan  
Republic of China  
March 31, 2017

**ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

We have at least one audit committee financial expert serving on the audit committee. The Board of Directors has determined that Mr. Lawrence Lin is the “audit committee financial expert” as defined in Item 16A of Form 20-F. We believe Mr. Lin is “independent” as defined in Rule 4200(a)(15) of the Marketplace Rules of the NASDAQ Stock Market.

#### ITEM 16B. CODE OF ETHICS

We have adopted the O<sub>2</sub>Micro International Limited Code of Business Conduct and Ethics (“Code of Conduct”), a code of business conduct and ethics that applies to our employees, officers and non-employee directors (including our principal executive officer, principal financial officer, principal accounting officer or controller), and persons performing similar functions. It is publicly available on our website at [www.o2micro.com](http://www.o2micro.com). If we make any substantive amendments or grant any waiver from a provision of the Code of Conduct to our directors or executive officers, we will disclose the nature of such amendment or waiver on that website or in a report on Form 6-K or in the next Annual Report on Form 20-F.

#### ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Deloitte & Touche has served as the Company's independent registered public accounting firm for each of the fiscal years in the two-year period ended December 31, 2016. The appointment of the independent registered public accounting firm is subject to approval and ratification by the Company's shareholders at the annual general meeting of shareholders. The following table presents the aggregate fees for professional services and other services rendered by Deloitte & Touche in each of the years ended December 31, 2016 and 2015.

	Year Ended December 31, 2016	Year Ended December 31, 2015
	<i>(in thousands)</i>	
Audit Fees	\$ 383	\$ 403
Audit-related Fees	10	10
Tax Fees	44	25
All other fees	-	30
Total	<u>\$ 437</u>	<u>\$ 468</u>

*Audit Fees.* This category includes the audit of our annual financial statements, review of quarterly financial statements, audit of our internal control over financial reporting and services that are normally provided by Deloitte & Touche in connection with statutory and regulatory filings or engagements for those fiscal years.

*Audit-related Fees.* This category consists of assurance and related services by Deloitte & Touche that are related to the performance of audit or review of our financial statements and are reported above under “Audit Fees.”

*Tax Fees.* This category consists of professional services rendered by Deloitte & Touche for tax compliance and tax consultation. The services for fees disclosed under this category include tax return preparation advice and technical tax consultation.

*All Other Fees.* This category consists of professional services rendered by Deloitte & Touche for fees in connection with COSO 2013 Integrated Framework preparation.

The audit committee pre-approves all audit and permissible non-audit services provided by the independent registered public accounting firm. These services may include audit services, audit-related services, tax services and other services. During the year ended December 31, 2016, the audit committee pre-approved all audit and non-audit-fees of Deloitte & Touche.

#### ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEE

Not applicable.

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

Period	Total Number of Shares Purchased (2)	Average Price Paid per Share (2)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1) (2) (3)	Maximum Number of Shares or Dollar of Value that May Yet Be Purchased Under the Plans or Programs (1) (2) (3)
January 1, 2016 to January 31, 2016	5,780,800	\$0.0291	5,780,800	\$9,881,703
February 1, 2016 to February 28, 2016	2,152,650	\$0.0283	2,152,650	\$9,820,778
March 1, 2016 to March 31, 2016	3,628,300	\$0.0299	3,628,300	\$9,712,237
April 1, 2016 to April 30, 2016	1,400,000	\$0.0296	1,400,000	\$9,670,792
May 1, 2016 to May 31, 2016	1,361,100	\$0.0294	1,361,100	\$9,630,816
June 1, 2016 to June 30, 2016	2,467,900	\$0.0304	2,467,900	\$9,555,694
July 1, 2016 to July 31, 2016	1,465,000	\$0.0310	1,465,000	\$9,510,290
August 1, 2016 to August 31, 2016	-	\$ -	-	\$9,510,290
September 1, 2016 to September 30, 2016	1,195,000	\$0.0322	1,195,000	\$9,471,824
October 1, 2016 to October 31, 2016	-	\$ -	-	\$9,471,824
November 1, 2016 to November 30, 2016	790,000	\$0.0371	790,000	\$9,442,515
December 1, 2016 to December 31, 2016	318,000	\$0.0382	318,000	\$9,430,370

(1) In May 2002, we announced a share repurchase program to repurchase up to 3,000,000 shares of our ADSs or 150,000,000 in ordinary shares after taking into account the 50-to-1 stock split on November 25, 2005. There is no expiration date for the share repurchase program.

(2) All share and price per share numbers reflect the 50-for-1 stock split which occurred on November 25, 2005.

(3) On November 14, 2005, our shareholders adopted a general mandate (the “Repurchase Mandate”) to exercise all the powers of our company to repurchase such number of ordinary shares not exceeding 10% of the total nominal amount of the share capital of our company in issue and to be issued. The Repurchase Mandate was to only become effective if and when our ordinary shares were listed for trading on the SEHK, which occurred on March 2, 2006.

(4) On June 30, 2010, our shareholders passed a resolution authorizing the purchase by the Company, in accordance with the provision of the Companies Law (2010 Revision) of the Cayman Islands of such of its own shares. No further Shareholder approval will be required in the future for the Company to repurchase its ordinary shares and the Board will have the authority to fix the number of share to be repurchased, as well as the price and other terms of any repurchase, as determined by the Board in its discretion from time to time. In July 2010, the Board approved that the Company adopt a plan to repurchase up to an aggregate of \$20.0 million of value of the Company’s issued and outstanding ordinary shares.

(5) In December 2011, our Board approved an additional \$30 million under our current program to repurchase the Company's ordinary shares. No date was established for the completion of the share repurchase program.

#### ITEM 16F. CHANGE IN REGISTRANT’S CERTIFYING ACCOUNTANT

Not applicable.

#### ITEM 16G. CORPORATE GOVERNANCE

We are a foreign private issuer whose ADSs are listed on the NASDAQ Global Market. As such, we are required to comply with U.S. federal securities laws, including the Sarbanes-Oxley Act, and the NASDAQ rules, including the NASDAQ corporate governance requirements. While we are generally in compliance with all of the NASDAQ corporate governance requirements, NASDAQ rules provide that foreign private issuers may follow home country practice in lieu of certain qualitative listing requirements subject to certain exceptions and except to the extent that such exemptions would be contrary to U.S. federal securities laws, so long as the foreign issuer discloses that it does not follow such listing requirement and describes the home country practice followed in its reports filed with the SEC. Below is a concise summary of the significant ways in which our corporate governance practices differ from the corporate governance requirements of NASDAQ applicable to domestic U.S. listed companies:

- We are not required under Cayman Islands law to, and do not, distribute interim reports directly to shareholders.

In addition, please also see Item 6 “Directors, Senior Management and Employees” and Item 10 “Additional Information” for further discussion on our corporate governance practices.

### PART III

#### ITEM 17. FINANCIAL STATEMENTS

The Company's Consolidated Financial Statements have been prepared in accordance with Item 18 hereof.

#### ITEM 18. FINANCIAL STATEMENTS

The Company's financial statements set forth in the accompanying Index to Consolidated Financial Statements included in this Annual Report on Form 20-F following Part IV beginning on page F-1 are hereby incorporated herein by this reference. Such consolidated financial statements are filed as part of this Annual Report on Form 20-F.

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2016 and 2015

Consolidated Statements of Operations and Comprehensive Income for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Shareholders' Equity for the years ended December 31, 2016, 2015 and 2014

Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014

Notes to Consolidated Financial Statements

#### ITEM 19. EXHIBITS

1. Amended and Restated Memorandum and Articles of Association of the registrant adopted pursuant to a special resolution passed on May 29, 2009, which took effect upon the withdrawal of the listing of the ordinary shares of the registrant on the Main Board of The Stock Exchange of Hong Kong Limited on September 9, 2009.
- 8.1 List of registrant's subsidiaries
- 12.1 Certification of Chief Executive Officer of the Company, pursuant to Section 302 of the Sarbanes-Oxley Act
- 12.2 Certification of Chief Financial Officer of the Company, pursuant to Section 302 of the Sarbanes-Oxley Act
13. Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act
- 15.1 Consent of Deloitte & Touche, independent registered public accounting firm

**SIGNATURES**

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this Annual Report on its behalf.

O<sub>2</sub>MICRO INTERNATIONAL LIMITED

Date: March 31, 2017

By: /s/ sterling du  
Name: Sterling Du  
Title: Chief Executive Officer

O<sub>2</sub>MICRO INTERNATIONAL LIMITED

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**O<sub>2</sub>Micro International Limited and Subsidiaries**

**Consolidated Financial Statements as of  
December 31, 2016 and 2015 and for the Three Years Ended December 31, 2016, 2015 and 2014, and  
Report of Independent Registered Public  
Accounting Firm**

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## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and the Shareholders of O<sub>2</sub>Micro International Limited:

We have audited the accompanying consolidated balance sheets of O<sub>2</sub>Micro International Limited and subsidiaries (the "Company") as of December 31, 2016 and 2015, and the related consolidated statements of operations and comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2016 (expressed in United States dollars). These 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 conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of O<sub>2</sub>Micro International Limited and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2016, based on the criteria established in *Internal Control - Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 31, 2017 expressed an unqualified opinion on the Company's internal control over financial reporting.

/s/ Deloitte & Touche  
Taipei, Taiwan  
Republic of China  
March 31, 2017

**O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**  
**(In Thousand US Dollars, Except Per Share Amounts and Share Data)**

ASSETS	December 31	
	2016	2015 As Adjusted (note 2)
<b>CURRENT ASSETS</b>		
Cash and cash equivalents (notes 4 and 5)	\$ 31,332	\$ 41,199
Restricted cash	32	31
Short-term investments (notes 4 and 6)	21,532	11,233
Accounts receivable, net	7,205	5,197
Inventories (note 7)	9,275	9,662
Prepaid expenses and other current assets (note 8)	1,106	1,100
Asset held for sale (note 10)	-	1,956
Total current assets	70,482	70,378
LONG-TERM INVESTMENTS (notes 4 and 9)	4,253	9,304
PROPERTY AND EQUIPMENT, NET (note 10)	13,736	14,011
OTHER ASSETS (note 11)	2,218	2,515
TOTAL ASSETS	\$ 90,689	\$ 96,208
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Notes and accounts payable	\$ 4,329	\$ 3,333
Income tax payable	180	2,245
Accrued expenses and other current liabilities (note 12)	4,102	4,896
Total current liabilities	8,611	10,474
<b>OTHER LONG-TERM LIABILITIES</b>		
Accrued pension liabilities (note 14)	281	272
Deferred income tax liabilities (notes 12 and 13)	930	2,206
Other liabilities (note 10)	83	139
Total long-term liabilities	1,294	2,617
Total liabilities	9,905	13,091
<b>COMMITMENTS AND CONTINGENCIES (notes 17 and 18)</b>		
<b>SHAREHOLDERS' EQUITY</b>		
Preference shares at \$0.00002 par value per share; Authorized – 250,000,000 shares;	-	-
Ordinary shares at \$0.00002 par value per share; Authorized – 4,750,000,000 shares; Issued – 1,669,036,600 and 1,660,786,600 shares as of December 31, 2016 and 2015, respectively Outstanding – 1,279,124,900 and 1,278,661,400 shares as of December 31, 2016 and 2015, respectively	33	33
Additional paid-in capital	142,738	141,886
Accumulated deficits	(41,372)	(38,386)
Accumulated other comprehensive income	4,415	4,824
Treasury stock – 389,911,700 and 382,125,200 shares as of December 31, 2016 and 2015, respectively	(25,030)	(25,240)
Total shareholders' equity	80,784	83,117
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 90,689	\$ 96,208

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

O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME  
(In Thousand US Dollars, Except Per Share Amounts and Share Data)

	Years Ended December 31		
	2016	2015	2014
NET SALES	\$ 56,561	\$ 54,841	\$ 63,591
COST OF SALES	27,317	27,145	30,856
GROSS PROFIT	29,244	27,696	32,735
OPERATING EXPENSES			
Research and development (a)	15,645	18,493	21,885
Selling, general and administrative (a)	19,481	23,632	24,721
Costs associated with exit activities (note 3)	-	-	3,027
Litigation income (note 18)	(23)	-	(75)
Total operating expenses	35,103	42,125	49,558
LOSS FROM OPERATIONS	(5,859)	(14,429)	(16,823)
NON-OPERATING INCOME			
Interest income	301	681	1,035
Foreign exchange gain, net	63	730	589
Impairment loss on long-term investments (note 9)	-	(4,953)	(83)
Gain on sale of long-term investments (note 9)	948	8	436
Gain on sale of real estate (note 10)	1,725	767	458
Other, net	894	741	515
Total non-operating income (loss)	3,931	(2,026)	2,950
LOSS BEFORE INCOME TAX	(1,928)	(16,455)	(13,873)
INCOME TAX EXPENSE (note 13)	1,058	4,640	1,184
NET LOSS	(2,986)	(21,095)	(15,057)
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX EFFECT OF NIL			
Foreign currency translation adjustments	(397)	(1,945)	(1,416)
Unrealized gain (loss) on available-for-sale investments (note 9)	1	-	(398)
Unrealized pension (loss) gain	(13)	1	70
Total other comprehensive loss	(409)	(1,944)	(1,744)
COMPREHENSIVE LOSS	\$ (3,395)	\$ (23,039)	\$ (16,801)

(Continued)

O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME  
(In Thousand US Dollars, Except Per Share Amounts and Share Data)

	Years Ended December 31		
	2016	2015	2014
LOSS PER SHARE (note 16)			
Basic and diluted	\$ -	\$ (0.02)	\$ (0.01)
NUMBER OF SHARES USED IN LOSS PER SHARE CALCULATION:			
Basic and Diluted (in thousands)	1,282,141	1,301,465	1,362,465
(a) INCLUDES STOCK-BASED COMPENSATION CHARGE AS FOLLOWS:			
Research and development	\$ 231	\$ 322	\$ 489
Selling, general and administrative	\$ 1,375	\$ 1,590	\$ 1,631

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

(Concluded)

O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In Thousand US Dollars, Except Share Data)

	Ordinary Shares		Additional Paid – in Capital	Retained Earnings (Accumulated Deficits)	Accumulated Other Comprehensive Income			Treasury Stock	Shareholders' Equity	
	Shares	Amount			Unrealized Investment Gain (Loss)	Cumulative Translation Adjustment	Unrealized Pension Gain (Loss)			Total
BALANCE, DECEMBER 31, 2013	1,660,786,600	\$ 33	\$ 140,198	\$ (2,234)	\$ 398	\$ 8,302	\$ (188)	\$ 8,512	\$ (19,899)	\$ 126,610
Issuance of:										
Shares for exercise of stock options	796,900	-	44	-	-	-	-	-	-	44
Shares for Employee Stock Purchase Plan	5,284,800	-	258	-	-	-	-	-	-	258
Shares vested under restricted share units	12,903,400	-	-	-	-	-	-	-	-	-
Acquisition of treasury stock – 83,468,900 shares	-	-	-	-	-	-	-	-	(4,965)	(4,965)
Treasury stock reissued for:										
Exercise of stock options	(796,900)	-	(59)	-	-	-	-	-	59	-
Employee Stock Purchase Plan	(5,284,800)	-	(383)	-	-	-	-	-	383	-
Restricted share units	(12,903,400)	-	(949)	-	-	-	-	-	949	-
Stock-based compensation	-	-	2,120	-	-	-	-	-	-	2,120
Net loss for 2014	-	-	-	(15,057)	-	-	-	-	-	(15,057)
Pension gain	-	-	-	-	-	-	70	70	-	70
Foreign currency translation adjustments	-	-	-	-	-	(1,416)	-	(1,416)	-	(1,416)
Unrealized gain on available-for-sale investments	-	-	-	-	74	-	-	74	-	74
Reclassification adjustments for gain on available-for-sale securities included in net loss	-	-	-	-	(472)	-	-	(472)	-	(472)
BALANCE, DECEMBER 31, 2014	1,660,786,600	33	141,229	(17,291)	-	6,886	(118)	6,768	(23,473)	107,266
Issuance of:										
Shares for exercise of stock options	677,100	-	31	-	-	-	-	-	-	31
Shares for Employee Stock Purchase Plan	4,833,300	-	180	-	-	-	-	-	-	180
Shares vested under restricted share units	15,728,550	-	-	-	-	-	-	-	-	-
Acquisition of treasury stock – 69,838,000 shares	-	-	-	-	-	-	-	-	(3,233)	(3,233)
Treasury stock reissued for:										
Exercise of stock options	(677,100)	-	(47)	-	-	-	-	-	47	-
Employee Stock Purchase Plan	(4,833,300)	-	(328)	-	-	-	-	-	328	-
Restricted share units	(15,728,550)	-	(1,091)	-	-	-	-	-	1,091	-
Stock-based compensation	-	-	1,912	-	-	-	-	-	-	1,912
Net loss for 2015	-	-	-	(21,095)	-	-	-	-	-	(21,095)
Pension gain	-	-	-	-	-	-	1	1	-	1
Foreign currency translation adjustments	-	-	-	-	-	(1,945)	-	(1,945)	-	(1,945)
BALANCE, DECEMBER 31, 2015	1,660,786,600	33	141,886	(38,386)	-	4,941	(117)	4,824	(25,240)	83,117
Issuance of:										
Shares for exercise of stock options	84,750	-	2	-	-	-	-	-	-	2
Shares for Employee Stock Purchase Plan	2,881,350	-	73	-	-	-	-	-	-	73
Shares vested under restricted share units	18,056,150	-	-	-	-	-	-	-	-	-
Acquisition of treasury stock – 20,558,750 shares	-	-	-	-	-	-	-	-	(619)	(619)
Treasury stock reissued for:										
Exercise of stock options	(84,750)	-	(5)	-	-	-	-	-	5	-
Employee Stock Purchase Plan	(2,881,350)	-	(187)	-	-	-	-	-	187	-
Restricted share units	(9,806,150)	-	(637)	-	-	-	-	-	637	-
Stock-based compensation	-	-	1,606	-	-	-	-	-	-	1,606
Net loss for 2016	-	-	-	(2,986)	-	-	-	-	-	(2,986)
Pension loss	-	-	-	-	-	-	(13)	(13)	-	(13)
Foreign currency translation adjustments	-	-	-	-	-	(397)	-	(397)	-	(397)
Unrealized gain on available-for-sale investments	-	-	-	-	524	-	-	524	-	524
Reclassification adjustments for gain on available-for-sale securities included in net loss	-	-	-	-	(523)	-	-	(523)	-	(523)

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BALANCE, DECEMBER 31, 2016	<u>1,669,036,600</u>	<u>\$ 33</u>	<u>\$ 142,738</u>	<u>\$ (41,372)</u>	<u>\$ 1</u>	<u>\$ 4,544</u>	<u>\$ (130)</u>	<u>\$ 4,415</u>	<u>\$ (25,030)</u>	<u>\$ 80,784</u>
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The accompanying notes are an integral part of the consolidated financial statements.

O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousand US Dollars)

	Years Ended December 31		
	2016	2015	2014
<b>OPERATING ACTIVITIES</b>			
Net loss	\$ (2,986)	\$ (21,095)	\$ (15,057)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	1,682	2,446	3,718
Stock-based compensation	1,606	1,912	2,120
Loss on asset write-off	-	-	82
Inventory write-downs	1,527	913	1,538
Gain on sale of long-term investments	(948)	(8)	(436)
Impairment loss on long-term investments	-	4,953	83
Gain on disposal of property and equipment, net	(1,726)	(738)	(428)
Deferred income taxes	(1,231)	1,989	78
Other, net	-	-	(36)
Changes in operating assets and liabilities:			
Accounts receivable, net	(2,008)	1,592	3,235
Inventories	(1,140)	(1,933)	(2,963)
Prepaid expenses and other current assets	(6)	191	130
Deferred charges	(375)	(416)	(985)
Notes and accounts payable	996	1,202	(2,038)
Income tax payable	(2,065)	1,595	412
Accrued expenses and other current liabilities	(1,064)	(1,039)	577
Accrued pension liabilities	(4)	(11)	(12)
Other liabilities	(56)	(168)	(346)
Net cash used in operating activities	(7,798)	(8,615)	(10,328)
<b>INVESTING ACTIVITIES</b>			
Acquisition of:			
Short-term investments	(28,797)	(7,128)	(22,346)
Property and equipment	(673)	(724)	(1,004)
Decrease (increase) in:			
Restricted cash	-	132	(1)
Other assets	40	82	116
Proceeds from:			
Sale of short-term investments	18,331	16,755	34,333
Sale of long-term investments	5,999	537	1,304
Disposal of property and equipment	3,837	3,205	1,982
Net cash (used in) provided by investing activities	(1,263)	12,859	14,384
<b>FINANCING ACTIVITIES</b>			
Acquisition of treasury stock	(619)	(3,233)	(4,965)
Proceeds from:			
Exercise of stock options	2	31	44
Issuance of ordinary shares under the Employee Stock Purchase Plan	73	180	258
Net cash used in financing activities	(544)	(3,022)	(4,663)

(Continued)

**O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(In Thousand US Dollars)**

	Years Ended December 31		
	2016	2015	2014
EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATE	\$ (262)	\$ (1,092)	\$ (617)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(9,867)	130	(1,224)
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR	41,199	41,069	42,293
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	<u>\$ 31,332</u>	<u>\$ 41,199</u>	<u>\$ 41,069</u>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOWS</b>			
Cash paid for interest	\$ -	\$ -	\$ -
Cash paid for tax	<u>\$ 4,349</u>	<u>\$ 1,068</u>	<u>\$ 697</u>

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

(Concluded)



## **O<sub>2</sub>MICRO INTERNATIONAL LIMITED AND SUBSIDIARIES**

### **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Expressed in United States Dollars Unless Otherwise Noted)**

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#### **1. GENERAL**

##### **Business**

O<sub>2</sub>Micro, Inc. was incorporated in the state of California in the United States of America on March 29, 1995. In March 1997, O<sub>2</sub>Micro International Limited (the "Company") was formed in the Cayman Islands and all authorized and outstanding common stock, preferred stock, and stock options of O<sub>2</sub>Micro, Inc. were exchanged for the Company's ordinary shares, preference shares, and stock options with identical rights and preferences. O<sub>2</sub>Micro, Inc. became the Company's subsidiary after the share exchange. The Company designs, develops and markets innovative power management components for the Computer, Consumer, Industrial, Automotive and Communications markets.

The Company's ordinary shares ("Shares") were initially listed on The NASDAQ National Market ("NASDAQ") on August 23, 2000, and on the Cayman Islands Stock Exchange on February 1, 2001. At the Extraordinary General Meeting of Shareholders ("EGM") held on November 14, 2005, the shareholders approved a public global offering of the Company's Shares and the proposed listing of the Company's Shares on the Main Board of The Stock Exchange of Hong Kong Limited ("SEHK") and various matters related to the proposed listing and offering. Following the approval of these matters, the Company ceased trading its Shares on the NASDAQ, effected a 50-for-1 share split of Shares, created an American depositary share ("ADS") program for the ADSs to be quoted on the NASDAQ, and delisted the Shares from the NASDAQ on November 25, 2005. The Company commenced trading of ADSs on the NASDAQ on November 28, 2005, and subsequently listed the Shares on the SEHK on March 2, 2006, by way of introduction. On February 27, 2009, the Company submitted an application for the voluntary withdrawal of the listing of Shares on the Main Board of SEHK (collectively referred to as "Proposed Withdrawal") for reasons of cost and utility. The Company retained its existing primary listing of ADSs on the NASDAQ following the Proposed Withdrawal and for the foreseeable future. The Proposed Withdrawal was approved at the EGM held on May 30, 2009, and the listing of the Shares on SEHK was withdrawn on September 9, 2009.

The Company has incorporated various wholly-owned subsidiaries in the past, including, among others, O<sub>2</sub>Micro Electronics, Inc. ("O<sub>2</sub>Micro-Taiwan"), O<sub>2</sub>Micro International Japan Ltd. ("O<sub>2</sub>Micro-Japan"), and O<sub>2</sub>Micro (China) Co., Ltd. ("O<sub>2</sub>Micro-China"). O<sub>2</sub>Micro-Taiwan is engaged in operations and sales support services. O<sub>2</sub>Micro-Japan is engaged in sales support services. O<sub>2</sub>Micro-China and other subsidiaries are mostly engaged in research and development services.

#### **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

##### **Basis of Presentation**

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated on consolidation.

### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Significant accounting estimates reflected in the Company's consolidated financial statements include valuation allowance for deferred income tax assets, allowance for doubtful accounts, other-than-temporary impairment of securities, inventory valuation, useful lives for property and equipment, impairment of long-lived assets and identified intangible assets, allowances for sales returns, pension and uncertain tax liabilities, contingencies and stock-based compensation.

### **Concentration of Credit Risk**

Financial instruments that potentially subject the Company to a concentration of credit risk consist of cash, cash equivalents, short-term investments and accounts receivable. Cash is deposited with high credit quality financial institutions. For cash equivalents and short-term investments, the Company invests primarily in time deposits at the banks with good credit rating. For accounts receivable, the Company performs ongoing credit evaluations of its customers' financial condition and the Company maintains an allowance for doubtful accounts based upon a review of the expected collectability of individual accounts.

### **Fair Value of Financial Instruments**

The Company's financial instruments include cash and cash equivalents, restricted cash, accounts receivable, and notes and accounts payable. The carrying amounts approximate the fair value due to the short-term maturity of those instruments. Fair value of available-for-sale investments including short-term investments and long-term investments is based on quoted market prices. Long-term investments in private company equity securities are accounted for under the cost method because the Company does not exercise significant influence over the entities. The Company evaluates related information including operating performance, subsequent rounds of financing, advanced product development and related business plan in determining the fair value of these investments and whether an other-than-temporary decline in value exists.

### **Cash and Cash Equivalents**

The Company considers all highly liquid investments with maturities of not more than three months when purchased to be cash equivalents. Investments with maturities of more than three months are classified as short-term investments.

### **Restricted Cash**

The Company classifies deposits made for customs and cash pledged to a bank for the issuance of letters of credit as restricted cash. The deposits are classified as current assets if refundable within a twelve-month period from the balance sheet date.

### **Short-term Investments**

The Company maintains its excess cash in time deposits, government, corporate, or other agency bonds issued with high credit ratings. The specific identification method is used to determine the cost of securities sold, with realized gains and losses reflected in non-operating income and expenses. All the above-mentioned investments except for time deposits were classified as available-for-sale securities and were recorded at fair value. Unrealized gains and losses on these investments are included in accumulated other comprehensive income and loss as a separate component of shareholders' equity, net of any related tax effect, unless unrealized losses are deemed other-than-temporary. Unrealized losses are recorded as a charge to income when deemed other-than-temporary. There were no available-for-sale securities as of December 31, 2016 and 2015.

Investment transactions are recorded on the trade date.

## **Inventories**

Inventories are stated at the lower of standard cost or market value. The cost of inventories comprises cost of purchasing raw materials and where applicable, those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is determined on a currently adjusted standard basis, which approximates actual cost on a first-in, first-out basis. The Company assesses its inventory for estimated obsolescence or unmarketable inventory based upon management's assumptions about future demand and market conditions and writes down inventory as needed.

## **Long-term Investments**

Long-term investments in private companies over which the Company does not exercise significant influence are accounted for under the cost method. Management evaluates related information in determining whether an other-than-temporary decline in value exists. Factors indicative of an other-than-temporary decline include recurring operating losses, credit defaults and subsequent rounds of financing at an amount below the cost basis of the investment. The list is not all-inclusive and management periodically weighs all quantitative and qualitative factors in determining if any impairment loss exists.

Long-term investments in listed companies are classified as available-for-sale securities and are recorded at fair value. Unrealized gains and losses on these investments are included in accumulated other comprehensive income and loss as a separate component of shareholders' equity, net of any related tax effect, unless unrealized losses are deemed other-than-temporary. Unrealized losses are recorded as a charge to income when deemed other-than-temporary.

## **Property and Equipment**

Property and equipment are stated at cost less accumulated depreciation. Major additions and betterments are capitalized, while maintenance and repairs are expensed as incurred.

Depreciation is computed on a straight-line basis over estimated service lives that range as follows: buildings - 35 to 50 years, equipment - 3 to 7 years, furniture and fixtures - 3 to 7 years, leasehold improvements - the shorter of the estimated useful life or the lease term, which is 2 to 5 years, and transportation equipment - 5 years.

## **Assets held for sale**

The Company considers assets to be held for sale (a) when management or others having the authority to do so approve a plan to sell the assets, (b) the assets are available for immediate sale in their present condition, (c) the Company has initiated an active program to locate a buyer and other actions required to complete the plan to sell the assets, (d) consummation of the transactions is probable and is expected to qualify for recognition as a completed sale, within one year, (e) the assets are being actively marketed for sale at a price that is reasonable in relation to their current fair value, and (f) the significant changes to the plan to sell the assets are not expected to be made or the plan is not expected to be withdrawn. When property and equipment are classified as held for sale, the Company discontinues depreciating the assets and measures the assets at lower of their carrying amount and fair value less costs to sell.

## **Long-lived Asset Impairment**

The Company evaluates the recoverability of long-lived assets whenever events or changes in circumstances indicate the carrying value may not be recoverable. The carrying value of a long-lived asset is considered impaired when the anticipated undiscounted cash flows from the asset is separately identifiable and is less than the carrying value. If impairment occurs, a loss based on the excess of the carrying value over the fair value of the long-lived asset is recognized. Fair value is determined by reference to quoted market prices, if available, or discounted cash flows, as appropriate.

## **Treasury Stock**

The Company may retire ordinary shares repurchased under a share repurchase plan. Accordingly, upon retirement the excess of the purchase price over par value is allocated between additional paid-in capital and retained earnings based on the average issuance price of the shares repurchased. The Company may also determine not to retire ordinary shares repurchased for the purpose of reissuing them upon exercise of stock option, Employee Stock Purchase Plan, and release of restricted stock units ("RSUs"). The reissue cost of shares repurchased is determined by the moving average method. A repurchase of ADS is recorded as treasury stock until the Company completes the withdrawal of the underlying ordinary shares from the ADS program.

## **Revenue Recognition**

Revenue from product sales to customers, other than distributors, is recognized at the time of shipment and when title and right of ownership transfers to customers. The four criteria for revenue being realized and earned are the existence of evidence of sale, actual shipment, fixed or determinable selling price, and reasonable assurance of collectability.

Allowances for sales returns and discounts are provided at the time of the recognition of the related revenues on the basis of experience and these provisions are deducted from sales.

In certain limited instances, the Company sells its products through distributors. Since the title and risk have not been transferred upon shipment to distributors, the Company recognizes revenue on these sales only when these distributors sell the Company's products to third parties. Thus, products held by these distributors are included in the Company's inventory balance.

## **Freight Costs**

Costs of shipping and handling for delivery of the Company's products that are reimbursed by customers are recorded as revenue in the consolidated statements of operations and comprehensive income. Shipping and handling costs are charged to cost of sales as incurred.

## **Research and Development**

Research and development costs consist of expenditures incurred during the course of planned research and investigation aimed at the discovery of new knowledge and intellectual property that will be useful in developing new products or processes, or at significantly enhancing existing products or production processes as well as expenditures incurred for the design and testing of product alternatives or construction of prototypes. All expenditures related to research and development activities of the Company are charged to operating expenses when incurred.

## **Advertising Expenses**

The Company expenses all advertising and promotional costs as incurred. These costs were approximately \$734,000, \$782,000, and \$948,000 in 2016, 2015, and 2014, respectively. A portion of these costs was for advertising, which approximately amounted to \$236,000, \$236,000, and \$205,000 in 2016, 2015, and 2014, respectively.

## **Pension Costs**

For employees under defined contribution pension plans, pension costs are recorded based on the actual contributions made to employees' pension accounts. For employees under defined benefit pension plans, pension costs are recorded based on the actuarial calculation.

## **Government Grants**

Government grants received by the Company to assist with specific research and development activities are recognized as non-operating income. If the Company has an obligation to repay any of the funds provided by government grants regardless of the outcome of the research and development, the Company will estimate that obligation and recognize the amount as a liability.

## **Income Tax**

The provision for income tax represents income tax paid and payable for the current year plus the changes in the deferred income tax assets and liabilities during the relevant years. Deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carryforwards. The Company believes that uncertainty exists regarding the realizability of certain deferred income tax assets and, accordingly, has established a valuation allowance for those deferred income tax assets to the extent the realizability is not deemed to be more likely than not. Deferred income tax assets and liabilities are measured using enacted tax rates. The Company has classified deferred tax assets and liabilities as noncurrent on the consolidated balance sheets as of December 31, 2016 and 2015 as the Company has early adopted Accounting Standards Update ("ASU") 2015-17, Balance Sheet Classification of Deferred Taxes, on a retrospective basis.

The Company utilizes a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates it is more likely than not that the position will be sustained in a dispute with taxing authorities, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than 50% likely of being realized upon ultimate settlement.

#### **Stock-based Compensation**

The Company grants stock options to its employees and certain non-employees and estimates the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense ratably over the requisite service periods. The Company has elected to use the Black-Scholes option pricing model to determine the fair value of stock options on the date of grant. The Company also grants RSUs to its employees and the RSUs are measured based on the fair market value of the underlying stock on the date of grant.

#### **Foreign Currency Transactions**

The functional currency is the local currency of the respective entities. Foreign currency transactions are recorded at the rate of exchange in effect when the transaction occurs. Gains or losses, resulting from the application of different foreign exchange rates when cash in foreign currency is converted into the entities' functional currency, or when foreign currency receivable and payable are settled, are credited or charged to income in the period of conversion or settlement. At year-end, the balances of foreign currency monetary assets and liabilities are recorded based on prevailing exchange rates and any resulting gains or losses are credited or charged to income.

#### **Translation of Foreign Currency Financial Statements**

The reporting currency of the Company is the US dollar. Accordingly, the financial statements of the foreign subsidiaries are translated into US dollars at the following exchange rates: assets and liabilities - current rate on balance sheet date; shareholders' equity - historical rate; income and expenses - weighted average rate during the year. The resulting translation adjustment is recorded as a separate component of shareholders' equity.

#### **Comprehensive Income (Loss)**

Comprehensive income (loss) represents net income (loss) plus the results of certain changes in shareholders' equity during a period from non-owner sources.

#### **Legal Contingencies**

The Company is currently involved in various claims and legal proceedings. Periodically, the Company reviews the status of each significant matter and assesses the potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount can be estimated, the Company accrues a liability for the estimated loss. In view of uncertainties related to these matters, accruals are based only on the best information available at the time. As additional information becomes available, the Company reassesses the potential liability related to the pending claims and litigation and revises these estimates as appropriate. Such revisions in the estimates of the potential liabilities could have a material impact on the results of operations and financial position.

As part of its standard terms and conditions, the Company offers limited indemnification to third parties with whom it enters into contractual relationships, including customers; however, it is not possible to determine the range of the amount of potential liability under these indemnification obligations due to the lack of prior indemnification claims. These indemnifications typically hold third parties harmless against specified losses, such as those arising from a breach of representation or covenant, or other third party claims that the Company's products, when used for their intended purposes, infringe the intellectual property rights of such other third parties. These indemnifications are triggered by any claim of infringement of intellectual property rights brought by a third party with respect to the Company's products. The terms of these indemnifications may not be waived or amended except by written notice signed by both parties, and may only be terminated with respect to the Company's products.

## Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standard Board (“FASB”) issued a new standard related to revenue recognition. Under the new standard, recognition of revenue occurs when a customer obtains control of promised goods or services in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, the new standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. In August 2015, the FASB issued an amendment to defer the effective date. The new standard is effective for fiscal years beginning after December 15, 2017 and early adoption is permitted for annual reporting periods beginning after December 15, 2016. In March and April 2016, the FASB issued two accounting updates to clarify the implementation guidance on principal versus agent considerations, performance obligations and the licensing. In addition, the FASB issued another accounting update in May 2016 to address narrow-scope improvements to the guidance on collectability, noncash consideration, and completed contracts at transition and provides a practical expedient for contract modifications at transition. The new guidance is required to be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying it recognized at the date of initial application. The Company is currently evaluating this guidance, but does not expect the adoption to have a material effect on the Company’s consolidated financial statements.

In June 2014, the FASB issued an accounting update, which clarifies the accounting for share-based payments. The guidance requires that a performance target that affects vesting and that could be achieved after the requisite service period is treated as a performance condition. The guidance is effective for fiscal years beginning after December 15, 2015 and early adoption is permitted. The adoption of this guidance did not have a material impact on the Company’s results of operations, financial position or cash flow.

In August 2014, the FASB issued new standard related to the presentation of financial statements when there may be conditions or events that raise substantial doubt about the entity’s ability to continue as a going concern. This standard sets forth management’s responsibility to evaluate, each reporting period, whether there is substantial doubt about our ability to continue as a going concern, and if so, to provide related footnote disclosures. The standard is effective for fiscal years beginning after December 15, 2016 and early adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company’s results of operations, financial position or cash flow.

In February 2015, the FASB issued an accounting update to amend the consolidation analysis. All legal entities are subject to reevaluation under the revised consolidation model. The amendment is effective for fiscal years beginning after December 15, 2015 and early adoption is permitted. The adoption of this amendment did not have a material impact on the Company’s results of operations, financial position or cash flow.

In July 2015, the FASB issued an accounting update to simplify the measurement of inventory. The amendment requires the measurement of inventory at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amendment applies to inventories for which cost is determined by methods other than the last-in first-out and the retail inventory methods. This amendment is effective prospectively for annual periods beginning after December 15, 2016 and early application is permitted. The adoption of this amendment is not expected to have a material impact on the Company’s results of operations, financial position or cash flow.

In November 2015, the FASB issued an accounting update to simplify the presentation of deferred income taxes. The amendment requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this guidance. This amendment is effective prospectively or retrospectively for annual periods beginning after December 15, 2016 and early application is permitted. The Company has elected to adopt the amendment as of December 31, 2016, and the retrospective adoption is applied to prior reporting period presented. The adoption of this amendment did not have a material impact on the Company’s financial position. Prior to the adoption, current deferred income tax assets, noncurrent deferred income tax assets, and current deferred income tax liabilities for the year ended December 31, 2015 were \$26,000, \$203,000, and \$2,206,000, respectively. To early adopt ASU 2015-17, the Company has reclassified current deferred income tax asset of \$26,000 and current deferred income tax liabilities of \$2,206,000 to noncurrent deferred tax assets and noncurrent income tax liabilities, respectively. After the reclassification, the noncurrent deferred income tax assets and noncurrent income tax liabilities for the year ended December 31, 2015 were \$229,000 and \$2,206,000, respectively.

In January 2016, the FASB issued an accounting update regarding the subsequent measurement of equity investment. The amendment requires all equity investment to be measured at fair value with changes in the fair value recognized through net income other than those accounted for under equity method of accounting or those that result in consolidation of the investee. The amendment also simplifies the impairment assessment of equity investments without readily determinable fair value by requiring assessment for impairment qualitatively and eliminating the complexity of the other-than-temporary impairment guidance. For financial reporting, the amendment requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. In addition, for public company: the amendment eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; for nonpublic company: the amendment eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost. This amendment is effective for fiscal years beginning after December 15, 2017 and early application is prohibited. The adoption of this amendment is not expected to have a material impact on the Company's financial position, results of operations, cash flow and financial statement disclosures.

In February 2016, the FASB issued a new standard regarding leases. The new standard requires an entity to recognize assets and liabilities arising from a lease for both financing and operating leases other than that the entity elects the short-term lease recognition and measurement exemption. Qualitative and quantitative disclosures will be enhanced to better understand the amount, timing and uncertainty of cash flows arising from leases. This standard is effective for fiscal years beginning after December 15, 2018, and early adoption is permitted. The Company is currently evaluating the effect this standard will have on its financial position, results of operations, cash flow and financial statement disclosures.

In March 2016, the FASB issued an accounting update to simplify several aspects of the accounting for share-based payment award transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The amendment is effective for fiscal years beginning after December 15, 2016, and earlier adoption is permitted. The adoption of this amendment is not expected to have a material impact on the Company's financial position, results of operations, cash flow and financial statement disclosures.

In June 2016, the FASB issued an accounting update to amend the guidance on the impairment of financial instruments that are not measured at fair value through profit and loss. The amendment introduces a current expected credit loss (CECL) model based on expected losses rather than incurred losses to estimate credit losses on financial instruments measured at amortized cost and requires a broader range of reasonable and supportable information to estimate expected credit loss. In addition, under the amendment, an entity recognizes an allowance for expected credit losses on financial instruments measured at amortized cost and available-for-sale debt securities rather than the current methodology of delaying recognition of credit losses until it is probable a loss has been incurred. The amendment is effective for fiscal years beginning after December 15, 2019, and earlier adoption is permitted as of the fiscal years beginning after December 15, 2018. The adoption of the amendments is not expected to have a material impact on the Company's financial position, results of operations, cash flow and financial statement disclosures. .

In August 2016, the FASB issued an accounting update to clarify the following eight cash flow classification issues: (1) debt prepayment or debt extinguishment costs, (2) settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, (3) contingent consideration payments made after the acquisition date of a business combination, (4) proceeds received from the settlement of insurance claims, (5) proceeds received from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, (6) distributions received from equity method investees, (7) beneficial interests in securitization transactions, and (8) separately identifiable cash flows and application of the predominance principle. The amendment is an improvement to reduce the current and potential future diversity in practice. The amendment is effective for fiscal years beginning after December 15, 2017, and earlier adoption is permitted. In addition, the amendment should be applied using a retrospective transition method to each period presented. The adoption of the amendments is not expected to have a material impact on the Company's statement of cash flows.

In November 2016, the FASB issued an accounting update related to the classification and presentation of changes in restricted cash on the statement of cash flows. The amendment requires restricted cash or restricted cash equivalents should be included with cash and cash equivalent when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amendment is effective for fiscal years beginning after December 15, 2017, and early adoption is permitted. The Company is currently evaluating the impact that the adoption will have on its statement of cash flows.

### 3. EXIT ACTIVITIES

In December 2014, the Company determined to dissolve the Intelligent Power Group, one of the product lines of the Company's Integrated Circuit Group, which comprised of the IC products such as DC/DC controller ICs, battery charger controllers ICs, charger ICs, and LDO Regulator ICs. The actions taken to dissolve the Intelligent Power Group resulted in significantly reducing the developing activities of the Intelligent Power products, and terminating the related workforce.

For the year ended December 31, 2014, the Company recorded costs associated with exit activities of \$3,027,000, of which \$82,000 and \$2,945,000 were related to a loss on asset write-off and one-time employee termination benefits, respectively. The Company determined that those assets directly held/carried by the Intelligent Power Group provided no future benefit and recognized a loss on asset write-off, including property and equipment of \$24,000, and deferred charges of \$58,000. As of December 31, 2014, one-time employee termination benefits of \$2,945,000 were accrued and recorded as accrued expenses and other current liabilities on the balance sheet, which had been settled in 2015. No further transactions were occurred for the year ended December 31, 2016.

### 4. FAIR VALUE MEASUREMENTS

The Company measures its cash equivalents and marketable securities at fair value. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. The Company measures its cash equivalents and marketable securities at fair value. The Company also determines the fair value of long-term investments and long-lived assets whenever events or changes in circumstances indicate the carrying value may not be recoverable. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value:

Level 1 – Observable inputs such as quoted prices for identical instruments in active markets;

Level 2 – Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly;

Level 3 – Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value on recurring and nonrecurring bases were as follows:

(In Thousands)

	Fair Value Measurements at the End of the Reporting Period			Total	
	Level 1	Level 2	Level 3		
<b>Items measured at fair value on a recurring basis at December 31, 2016</b>					
Cash and cash equivalents					
Money market mutual funds	\$ -	\$ 162	\$ -	\$ 162	
<b>Items measured at fair value on a recurring basis at December 31, 2015</b>					
Cash and cash equivalents					
Money market mutual funds	\$ -	\$ 161	\$ -	\$ 161	
<b>Items measured at fair value on a nonrecurring basis at December 31, 2015 (nil at December 31, 2016)</b>					
	Level 1	Level 2	Level 3	Total	Total Losses
Long-term investments					
Cost method securities (note 9)	\$ -	\$ -	\$ 2,414	\$ 2,414	\$ (4,953)



The Company utilized a pricing service to estimate fair value measurements for the money market mutual funds. The pricing service utilized market quotations for fixed maturity securities that had quoted prices in active markets. Fixed maturity securities generally traded daily on dealer bids rather than bids recorded on exchanges. The pricing service prepared estimates of fair value measurements for these securities using its proprietary pricing applications which included available relevant market information, benchmark curves, benchmarking of like securities, sector groupings and matrix pricing. Since most of the fixed maturity securities had maturities of one year or less, the Company believed that the fair value would not be materially different from the original purchased cost. The Company's fair value processes included controls that were designed to ensure appropriate fair values were recorded. Such controls, which may be performed quarterly or when certain assets need to be measured at fair value on a non-recurring basis, include a detailed review of methodologies and assumptions and a management review of valuation.

The fair value estimates provided by the pricing service for the Company's investments were based on observable market information rather than market quotes. Accordingly, the estimates of fair value for short-term investments were determined based on Level 2 inputs at December 31, 2016 and 2015, respectively.

The fair value measurement in cost method securities was determined based on certain evidential financial information. Please also see discussions in note 9.

## 5. CASH AND CASH EQUIVALENTS

(In Thousands)

	December 31	
	2016	2015
Time deposits	\$ 2,289	\$ 8,616
Savings and checking accounts	28,873	32,414
Money market mutual funds	162	161
Petty cash	8	8
	<u>\$ 31,332</u>	<u>\$ 41,199</u>

## 6. SHORT-TERM INVESTMENTS

(In Thousands)

	December 31, 2016			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Time deposits	\$ 21,532	\$ -	\$ -	\$ 21,532

  

	December 31, 2015			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Time deposits	\$ 11,233	\$ -	\$ -	\$ 11,233

Short-term investments by contractual maturity were as follows:

**(In Thousands)**

	<b>December 31, 2016</b>	
	<b>Cost</b>	<b>Fair Value</b>
Time deposits		
Due within one year	\$ 21,504	\$ 21,504
Due after one year through two years	28	28
	<u>\$ 21,532</u>	<u>\$ 21,532</u>

**(In Thousands)**

	<b>December 31, 2015</b>	
	<b>Cost</b>	<b>Fair Value</b>
Time deposits		
Due within one year	\$ 11,205	\$ 11,205
Due after one year through two years	28	28
	<u>\$ 11,233</u>	<u>\$ 11,233</u>

The Company's gross realized gains and losses on the sale of investments for the years ended December 31, 2016 and 2015 were both \$0. The Company's gross realized gains and losses on the sale of investments for the year ended December 31, 2014 were \$38,000 and \$2,000, respectively.

## 7. INVENTORIES

**(In Thousands)**

	<b>December 31</b>	
	<b>2016</b>	<b>2015</b>
Finished goods	\$ 2,586	\$ 3,080
Work-in-process	3,341	1,847
Raw materials	3,348	4,735
	<u>\$ 9,275</u>	<u>\$ 9,662</u>

## 8. PREPAID EXPENSES AND OTHER CURRENT ASSETS

(In Thousands)

	December 31	
	2016	2015 As Adjusted (note 2)
Prepaid expenses	\$ 420	\$ 545
Other receivable	368	158
Payment in advance	202	230
Interest receivable	48	94
Other	68	73
	<u>\$ 1,106</u>	<u>\$ 1,100</u>

## 9. LONG-TERM INVESTMENTS

(In Thousands)

	December 31	
	2016	2015
Cost method		
Sigurd Microelectronics (Cayman) Co., Ltd. ("Sigurd Cayman")	\$ 2,365	\$ 2,365
X-FAB Silicon Foundries SE ("X-FAB")	-	4,968
Philip Ventures Enterprise Fund ("PVEF")	44	49
GEM Services, Inc. ("GEM")	-	78
Excelliance MOS Co., Ltd ("EMC")	1,844	1,844
Verticil Electronics Corp. ("Verticil")	-	-
Asia Sinomos Semiconductor Inc. ("Sinomos")	-	-
Silicon Genesis Corporation ("SiGen")	-	-
	<u>4,253</u>	<u>9,304</u>
Available-for-sale securities – noncurrent		
Etrend Hightech Corp. ("Etrend")	-	-
	<u>\$ 4,253</u>	<u>\$ 9,304</u>

The following table shows the movement of gross unrealized gains and losses of the Company's available-for-sale securities.

(In Thousands)

	Years Ended December 31		
	2016	2015	2014
Balance at beginning of period	\$ -	\$ -	\$ 398
Other comprehensive income before reclassification adjustment	523	-	74
Reclassification adjustment	(523)	-	(472)
Balance at end of period	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

In July 2008, the Company invested in preferred shares of Sigurd Cayman for \$5,700,000 to become a strategic partner of Sigurd Microelectronics Corporation ("Sigurd"). Upon completion of the transaction, the Company obtained a 19.54% ownership of Sigurd Cayman. The Company accounts for the investment under the cost method as the Company does not exercise significant influence over operating and financial policies of Sigurd Cayman and management of Sigurd holds the controlling interests. In April 2010, the Company participated in another round of preferred shares issued by Sigurd Cayman amounting to \$1,500,000. In September 2015, Sigurd Cayman announced the liquidation of its wholly owned subsidiary, Sigurd Microelectronics (Wuxi) Co., Ltd. ("Sigurd Wuxi"), whose sales and operations account for the majority business of Sigurd Cayman. In view of Sigurd Cayman's recurring financial losses and its decision to cease operations of Sigurd Wuxi, the Company determined that the decline in fair value of the investment in Sigurd Cayman was other-than-temporary and recognized an impairment charge of \$4,835,000 in 2015. The resulting investment which was classified as Level 3 in the fair value hierarchy was valued using a discounted cash flow model considering the latest available financial information which primarily consists of cash and time deposits. The valuation inputs primarily included an estimate of future cash flows, expectations about possible variations in the amount and timing of cash flows. The significant unobservable input is assumed no future revenue and cost associated with production activities. As of December 31, 2016, the Company held 9,690,445 shares, which represented an 18.88% ownership of Sigurd Cayman.

The Company invested in X-FAB's ordinary shares in July 2002. X-FAB (formerly known as X-FAB Semiconductor Foundries AG) is a European-American foundry group that specializes in analog/mixed-signal application. As of December 31, 2015, the Company held 530,000 shares at the cost of \$4,968,000 (4,982,000 EURO), which represented a 1.60% ownership of X-FAB. In April 2016, the Company sold the entire X-FAB's ordinary shares to a third party company and a gain of \$413,000 was recorded for the year ended December 31, 2016.

In November 2005, the Company invested in PVEF, a fund management company in Singapore, with an investment amount of \$585,000 (SG\$1,000,000) for 20 units in the placement at SG\$50,000 per unit. The Company further invested \$357,000 (SG\$500,000) in June 2010 to obtain 30 units. A portion of the shares were redeemed by PVEF in November 2012 and May 2015 at a cost of \$445,000 and \$330,000, respectively, and the carrying cost of the Company is reduced to \$167,000 accordingly. In December 2015, in view of the fund's liquidation and continuous lower net asset value than the cost, the Company determined that the decline in fair value of the investment in PVEF was other-than-temporary and recognized an impairment charge of \$118,000. The fair value for the fund was estimated based on the net asset value of the Company's ownership interest in the fund due to the fact that distributions from fund will be received through the liquidation of the underlying assets of the fund or the redemption of shares initiated by the fund and there were no unfunded commitments as of December 31, 2015. The investment was classified as Level 3 in the fair value hierarchy as the fund was redeemable at December 31, 2015. The Company held a 5% interest in the fund as of December 31, 2016.

The Company invested in GEM's preference shares in August 2002. GEM is a multinational semiconductor assembly and test company. On April 16, 2012, GEM signed a share purchase agreement with a listed company in Taiwan which will purchase GEM's preference share at a price of \$0.235 per share to obtain approximately 58.4% ownership of GEM. In respect to this subsequent event, the Company considered this a Type I subsequent event and the investment to be other-than-temporarily impaired. Therefore, the Company recognized an impairment loss of \$422,000 as of December 31, 2011. As of December 31, 2015, the Company held 333,334 shares at the cost of \$78,000, which represented a 0.35% ownership of GEM. In April 2016, GEM was successfully listed on the Taiwan Stock Exchange and as such investment was classified as available-for-sale. In the third quarter of 2016, the Company sold the entire GEM's shares in the stock exchange market and a gain of \$523,000 was recorded for the year ended December 31, 2016.

The Company invested \$1,960,000 (NT\$62,900,000) in EMC's 3,468,000 ordinary shares in June 2010. EMC is a fabless power device design company in Taiwan, specialized in power semiconductor process development, and the design of high efficiency power device and system. In December 2012, the Company sold 200,000 shares in the amount of \$138,000 in the process of EMC's getting listed on the Emerging Stock GreTai Security Market of Taiwan. As of December 31, 2016, the Company held 3,474,854 shares at the cost of \$1,844,000, which represented an 11.15% ownership of EMC.

In July 2013, the Company invested \$250,000 (NT\$7,500,000) in Verticil, a privately-owned manufacturer of LED power modules and integrated lighting solutions provider in Taiwan. Based on the recent operating status and a round of financing of Verticil in August 2014, the Company considered the investment to be other-than-temporarily impaired. Therefore, the Company recognized an impairment loss of \$83,000 (NT\$2,500,000) in the third quarter of 2014. The Company sold the entire Verticil shares during the second half of 2015 and a gain of \$8,000 was recorded for the year ended December 31, 2015.

The Company invested in Etrend's ordinary shares in December 2002, July 2003, and March 2004, respectively. Etrend is a wafer probing, packing and testing company. In August 2007, Etrend's shares were listed on the Emerging Stock GreTai Security Market of Taiwan and the Company reclassified the investment in Etrend to available-for-sale securities. Etrend was successfully listed on the GreTai Securities Market of Taiwan in November 2010. The Company sold the entire Etrend shares in the stock exchange market during the second half of 2014 and a gain of \$436,000 was recorded for the year ended December 31, 2014.

In January 2005, the Company invested in ordinary shares of Sinomos, a privately owned foundry company, at a total amount of \$5,000,000. In May and December 2006, the Company further invested in preferred shares of \$3,288,000 and \$4,785,000, respectively. In September 2008, in view of Sinomos' operating status and recurring financial losses, the Company determined that the decline in fair value of the investment in Sinomos was other-than-temporary and recognized an impairment charge of \$13,073,000. Along with the recognition of impairment charge, the Company also wrote-off the outstanding prepayments in relation to Sinomos' foundry service of \$2,942,000. As of December 31, 2016, the Company held 30,101,353 of ordinary and preference shares, representing an 18.41% ownership of Sinomos.

The Company invested in SiGen preferred shares in December 2000. SiGen is an advanced nanotechnology company that develops Silicon-on-insulator, stained-silicon products and other engineered multi-layer structures to microelectronics and photonic for advanced electronic and opto-electronic device applications. In 2002 and 2003, the Company reviewed qualitative factors related to the investment, determined that the decline in value was other-than-temporary and the carrying value was decreased to zero. The Company held 23,946 shares of SiGen as of December 31, 2016, representing a 0.06% ownership of SiGen.

## 10. PROPERTY AND EQUIPMENT, NET

(In Thousands)

	December 31	
	2016	2015
<b>Cost</b>		
Land	\$ 2,510	\$ 2,510
Buildings	6,066	6,066
Equipment	21,284	21,819
Furniture and fixtures	779	826
Leasehold improvements	2,135	1,785
Transportation equipment	657	698
Property leased to others	3,944	3,875
Prepayment for property and equipment	1,629	1,863
	<u>39,004</u>	<u>39,442</u>
<b>Accumulated depreciation</b>		
Buildings	1,667	1,526
Equipment	20,521	20,965
Furniture and fixtures	733	744
Leasehold improvements	1,536	1,474
Transportation equipment	610	619
Property leased to others	201	103
	<u>25,268</u>	<u>25,431</u>
	<u>\$ 13,736</u>	<u>\$ 14,011</u>

Depreciation expense recognized during the years ended December 31, 2016, 2015, and 2014, was approximately \$1,103,000, \$1,730,000, and \$2,548,000, respectively.

As a result of dissolution activities of the Intelligent Power Group, a loss on asset write-off of \$24,000 on property and equipment was incurred for the year ended December 31, 2014. Please see discussions in note 3.

In August 2009, the Company sold its land, located in Hsinchu, Taiwan, to a real estate developer in exchange for a portion of the real estate after it is developed, which includes a portion of an office building and a portion of a parking lot, with a carrying value of approximately \$8,918,000. The Company consummated this transaction to acquire office building space and parking lot space for the purpose of future operations and business growth. The Company deferred the transaction gain of \$129,000 during the construction period. Since the fourth quarter of 2014, the title of some units of the buildings were completed and sold to the third party and the Company has realized the deferred gain of \$106,000 accordingly. Considering the Company's current operating scale and capital requirements, the Company leased out three units to a third party in December 2014. The Company has also sold 5 building units to third parties since the fourth quarter of 2014. As a result of the sale of building units, net gains of \$767,000 and \$458,000 were recorded for the years ended December 31, 2015 and 2014, respectively. No building unit transactions were occurred for the year ended December 31, 2016.

Beginning in November 2015, the Company has negotiated with a third party company to dispose one of the three units of the Company's office building located in China. A letter of intent has also been signed by both parties in January 2016. The Company determined that this transaction met the criteria of asset held for sale and such reclassification was made as of December 31, 2015. The transaction was subsequently completed in the third quarter of 2016 and a net gain of \$1,725,000 was recorded for the year ended December 31, 2016.

## 11. OTHER ASSETS

(In Thousands)

	December 31	
	2016	2015 As Adjusted (note 2)
Deferred charges	\$ 867	\$ 1,060
Land use rights	724	743
Refundable deposits	443	483
Deferred income tax assets – noncurrent	184	229
	<u>\$ 2,218</u>	<u>\$ 2,515</u>

Deferred charges are advanced payments for consulting, maintenance, and engineering license contracts and are amortized over the terms of the contracts from 2 to 5 years. Amortization expense of the deferred charges for the years ended December 31, 2016, 2015, and 2014, was approximately \$560,000, \$688,000, and \$1,142,000, respectively.

As a result of dissolution activities of the Intelligent Power Group, loss on asset write-off of \$58,000 on deferred charges was incurred for the year ended December 31, 2014. Please see discussions in note 3.

All land within municipal zones in China is owned by the government. Limited liability companies, joint stock companies, foreign-invested enterprises, privately held companies and individual natural persons must pay fees for granting of rights to use land within municipal zones. Legal use of land is evidenced and sanctioned by land use certificates issued by the local municipal administration of land resources. Land use rights granted for industrial purposes are limited to a term of no more than 50 years.

Land use rights are recorded at cost less accumulated amortization. Amortization is provided on a straight-line basis over the term of the land use rights agreement which is 49.7 years. Amortization expense of the land use rights for the years ended December 31, 2016, 2015, and 2014, was approximately \$19,000, \$28,000, and \$28,000, respectively.

## 12. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

(In Thousands)

	December 31	
	2016	2015 As Adjusted (note 2)
Salaries, bonus and benefits	\$ 2,235	\$ 2,305
Engineering related expenses	641	630
Payable for acquisition of equipment	277	32
Legal and audit fees	251	361
Withholding tax payable	86	100
Shipping expenses	74	146
Promotional expenses	66	35
Value-added tax payable	36	27
Consulting fees	5	366
Other accrued expenses	431	894
	<u>\$ 4,102</u>	<u>\$ 4,896</u>

### 13. INCOME TAX

The Company is not subject to income or other taxes in the Cayman Islands. However, subsidiaries are subject to taxes of the jurisdiction where they are located.

Loss before income taxes consisted of:

	(In Thousands)		
	Years Ended December 31		
	2016	2015	2014
Cayman Islands	\$ (4,156)	\$ (19,183)	\$ (18,943)
Foreign	2,228	2,728	5,070
	<u>\$ (1,928)</u>	<u>\$ (16,455)</u>	<u>\$ (13,873)</u>

Income tax expense consisted of:

	(In Thousands)		
	Years Ended December 31		
	2016	2015	2014
Current	\$ 2,289	\$ 2,651	\$ 1,106
Deferred	(1,231)	1,989	78
Income tax expense	<u>\$ 1,058</u>	<u>\$ 4,640</u>	<u>\$ 1,184</u>

The Company and its subsidiaries file separate income tax returns. The applicable statutory income tax rate in the Cayman Islands was zero for the Company for the years being reported. The reconciliation between the provision for income taxes at the statutory rate and the provision for income taxes at the effective tax rate is as follows:

	(In Thousands)		
	Years Ended December 31		
	2016	2015	2014
Tax expense at statutory rate	\$ -	\$ -	\$ -
Increase (decrease) in tax resulting from:			
Differences between Cayman and foreign tax rates	449	675	989
Changes in deferred income tax assets and liabilities	(1,249)	1,976	(72)
Adjustments to prior years' taxes	33	20	23
Changes in valuation allowances for deferred income tax assets	18	13	150
Withholding taxes on repatriation of subsidiary profits	1,669	1,757	-
Other	138	199	94
	<u>\$ 1,058</u>	<u>\$ 4,640</u>	<u>\$ 1,184</u>

The deferred income tax assets and liabilities as of December 31, 2016 and 2015 consisted of the following:

(In Thousands)

	December 31	
	2016	2015
<b>Deferred income tax assets</b>		
Research and development credits	\$ 5,979	\$ 5,933
Net operating loss carryforwards	161	195
Depreciation and amortization	269	277
Accrued vacation and other expenses	25	56
	<u>6,434</u>	<u>6,461</u>
Valuation allowance	(6,250)	(6,232)
<b>Total net deferred income tax assets</b>	<u>\$ 184</u>	<u>\$ 229</u>
<b>Deferred income tax liabilities</b>		
Withholding taxes on repatriation of subsidiary profits	\$ 920	\$ 2,188
Unrealized foreign exchanges	10	18
	<u>\$ 930</u>	<u>\$ 2,206</u>

The valuation allowance shown in the table above relates to net operating losses, credit carryforwards and temporary differences for which the Company believes that realization is not more than likely. The valuation allowance increased by \$18,000, \$13,000, and \$150,000 for the years ended December 31, 2016, 2015, and 2014, respectively. The changes in the valuation allowance in 2016, 2015, and 2014, were primary due to the fluctuations in R&D credits from O<sub>2</sub>Micro Inc. that could not be utilized.

As of December 31, 2016, O<sub>2</sub>Micro, Inc. had U.S. federal and state research and development credit carryforwards of approximately \$5,284,000 and \$6,840,000, respectively. The US federal research and development credit will expire from 2022 through 2036 if not utilized, while the state research and development credit will never expire. Utilization of the research and development credits may be subject to significant annual limitation due to the ownership change limitations provided by the U.S. Internal Revenue Code of 1986 and similar provisions in the State of California's tax regulations. The annual limitation may result in the expiration of federal research and development credits before utilization.

As of December 31, 2016, the Company's subsidiary had U.S. net operating loss carryforwards for federal and state tax purpose of \$383,000 and \$526,000, respectively, which will expire, if not utilized beginning in 2033 and 2028.

To better position itself for the future growth phase, the Company considered the repatriation of the earnings from subsidiaries in Taiwan and China beginning in the second quarter of 2015. As a result, deferred tax liabilities from withholding tax for the unremitted earnings in Taiwanese and Chinese subsidiaries have been recorded for \$920,000 and \$2,188,000 as of December 31, 2016 and 2015, respectively.

The Company files income tax returns in various foreign jurisdictions. The Company is generally no longer subject to income tax examinations by tax authorities for years prior to 2011 because of the statute of limitations.

#### 14. RETIREMENT AND PENSION PLANS

The Company has a savings plan that qualifies under Section 401(k) of the US Internal Revenue Code. Participating employees may defer up to the US Internal Revenue Service statutory limit amounts of pretax salary. The Company may make voluntary contributions to the savings plan but has made no contributions since the inception of the savings plan in 1997.



The Company also participates in mandatory pension funds and social insurance schemes, if applicable, for employees in jurisdictions in which other subsidiaries or offices are located to comply with local statutes and practices. For the years ended December 31, 2016, 2015, and 2014, pension costs charged to income in relation to the contributions to these schemes were \$984,000, \$1,152,000, and \$1,328,000, respectively. The Company adopted a defined benefit pension plan and established an employee pension fund committee for certain employees of O<sub>2</sub>Micro-Taiwan who are subject to the Taiwan Labor Standards Law (“Labor Law”) to comply with local requirements. This benefit pension plan provides benefits based on years of service and average salary computed based on the final six months of employment. The Labor Law requires the Company to contribute between 2% to 15% of employee salaries to a government specified plan, which the Company currently makes monthly contributions equal to 2% of employee salaries. Contributions are required to be deposited in the name of the employee pension fund committee with the Bank of Taiwan.

The government is responsible for the administration of all the defined benefit plans for the companies in Taiwan under the Labor Standards Law. The government also sets investment policies and strategies, determines investment allocation and selects investment managers. As of December 31, 2016 and 2015, the asset allocation was primarily in cash, equity securities and debt securities. Furthermore, under the Labor Standards Law, the rate of return on assets shall not be less than the average interest rate on a two-year time deposit published by the local banks and the government is responsible for any shortfall in the event that the rate of return is less than the required rate of return. However, information on how investment allocation decisions are made, inputs and valuation techniques used to measure the fair value of plan assets, the effect of fair value measurements using significant unobservable inputs on changes in plan assets for the period and significant concentrations of risk within plan assets is not fully made available to the companies by the government. Therefore, the Company is unable to provide the required fair value disclosures related to pension plan assets.

The percentage of major category of plan assets as of December 2016 and 2015 were as follows:

	<u>December 31</u>	
	2016	2015
Cash	18%	17%
Debt securities	30%	30%
Equity securities	45%	50%

Changes in projected benefit obligation and plan assets for the years ended December 31, 2016 and 2015 were as follows:

	<b>(In Thousands)</b>		
	<u>Years Ended December 31</u>		
	2016	2015	2014
Projected benefit obligation, beginning of the year	\$ 838	\$ 838	\$ 933
Service cost	3	3	3
Interest cost	13	16	17
Benefits paid	-	-	-
Actuarial (gain) loss	8	11	(61)
Effect of changes in foreign exchange rate	15	(30)	(54)
Projected benefit obligation, end of the year	<u>\$ 877</u>	<u>\$ 838</u>	<u>\$ 838</u>
Fair value of plan assets, beginning of the year	\$ 566	\$ 545	\$ 542
Employer contributions	16	27	24
Actual return on plan assets	4	14	12
Effect of changes in foreign exchange rate	10	(20)	(33)
Fair value of plan assets, end of the year	<u>\$ 596</u>	<u>\$ 566</u>	<u>\$ 545</u>

The component of net periodic benefit cost was as follows:

	Years Ended December 31		
	2016	2015	2014
Service cost	\$ 3	\$ 3	\$ 3
Interest cost	13	16	17
Expected return on plan assets	(10)	(9)	(9)
Amortization of net pension loss	1	6	6
Net periodic benefit cost	<u>\$ 7</u>	<u>\$ 16</u>	<u>\$ 17</u>

The funded status of the plan was as follows:

	December 31	
	2016	2015
Accumulated benefit obligation	<u>\$ (714)</u>	<u>\$ (672)</u>
Project benefit obligation	(877)	(838)
Plan assets at fair value	<u>596</u>	<u>566</u>
Funded status of the plan	<u>\$ (281)</u>	<u>\$ (272)</u>

The actuarial assumptions to determine the benefit obligations were as follows:

	December 31	
	2016	2015
Discount rate	1.5%	1.5%
Rate of compensation increases	2.0%	2.0%

The actuarial assumptions to determine the net periodic benefit cost were as follows:

	Years Ended December 31		
	2016	2015	2014
Discount rate	1.5%	2.0%	2.0%
Rate of compensation increases	2.0%	2.0%	2.0%
Expected long-term rate of return on plan assets	1.8%	1.8%	1.8%

The expected long-term rate of return shown for the plan assets was weighted to reflect a two-year deposit interest rate of local banking institutions.

Estimated future benefit payments are as follows:

	(In Thousands)
<b>Year</b>	
2017	\$ 13
2018	20
2019	15
2020	37
2021 and thereafter	389

## 15. STOCK-BASED COMPENSATION

### Employee Stock Purchase Plan

In October 1999, the Board adopted the 1999 Employee Stock Purchase Plan (“1999 Purchase Plan”), which was approved by the shareholders prior to the consummation of its initial public offering in August 2000. A total of 50,000,000 ordinary shares were reserved for issuance under the 1999 Purchase Plan, plus annual increases on January 1 of each year, commencing in 2001, up to 40,000,000 shares as approved by the Board. In June 2008, an additional 20,000,000 shares were reserved for issuance as also approved by the Board. The 1999 Purchase Plan was subject to adjustment in the event of a stock split, stock dividend or other similar changes in ordinary shares or capital structure.

The 1999 Purchase Plan permitted eligible employees to purchase ordinary shares through payroll deductions, which may range from 1% to 10% of an employee’s regular base pay. Beginning November 1, 2005, the 1999 Purchase Plan was implemented through consecutive offer periods of 3 months’ duration commencing on the first day of February, May, August and November. Under the 1999 Purchase Plan, ordinary shares may be purchased at a price equal to the lesser of 90% of the fair market value of the Company’s ordinary shares on the date of grant of the option to purchase (which is the first day of the offer period) or 90% of the fair market value of the Company’s ordinary shares on the applicable exercise date (which is the last day of the offer period). Employees may have elected to discontinue their participation in the purchase plan at any time; however, all of the employee’s payroll deductions previously credited to the employee’s account will be applied to the exercise of the employee’s option on the next exercise date. Participation ends automatically on termination of employment with the Company. If not terminated earlier, the 1999 Purchase Plan had a term of 10 years. By 2009, 10,685,400 ordinary shares had been purchased under the 1999 Purchase Plan.

As approved by the EGM held on May 30, 2009, the Company adopted the 2009 Employee Stock Purchase Plan (“2009 Purchase Plan”) along with the Company delisting from SEHK in September 2009. The 2009 Purchase Plan succeeded the 1999 Purchase Plan, and the terms and provisions of 2009 Purchase Plan are generally the same as the 1999 Purchase Plan. The 2009 Purchase Plan has a term of 10 years, if not terminated earlier. A total of 25,000,000 ordinary shares were reserved for issuance under the 2009 Purchase Plan starting November 2009. As approved by the Annual General Meeting of Shareholders (“AGM”) held on June 22, 2012, additional 15,000,000 ordinary shares were reserved for issuance under the 2009 Purchase Plan. From 2014 to 2016, 12,999,450 ordinary shares had been purchased under the 2009 Purchase Plan.

### Stock Option Plans

In 1997, the Board adopted the 1997 Stock Plan, and in 1999, adopted the 1999 Stock Incentive Plan. The plans provide for the granting of stock options to employees, directors and consultants of the Company.

Under the 1997 Stock Plan, the Board reserved 185,000,000 ordinary shares for issuance. After the completion of an initial public offering, no further options were granted under the 1997 Stock Plan. Under the 1999 Stock Incentive Plan, the maximum aggregate number of shares available for grant was 150,000,000 ordinary shares plus an annual increase on January 1 of each year, which commenced in 2001, equal to the lesser of 75,000,000 shares or 4% of the outstanding ordinary shares on the last day of the preceding fiscal year or a smaller number determined by the plan administrator. As of December 31, 2016, the number of stock options outstanding and exercisable was both 0 under the 1999 Stock Incentive Plan.

The Board adopted the 2005 Share Option Plan (“2005 SOP”), which was effective on March 2, 2006, the date the Company completed the listing on the SEHK. The adoption of the 2005 SOP also resulted in the Board terminating the 1997 Stock Plan and 1999 Stock Incentive Plan. The Company began issuing stock options solely under the 2005 SOP for up to 100,000,000 ordinary shares. As approved by the EGM held on May 30, 2009, the number of shares available for issue was increased from 100,000,000 to 175,000,000 shares. The references to Hong Kong and Hong Kong related rules and regulations were also removed along with the completion of the Company’s delisting from the SEHK in 2009. As approved by the AGM held on June 22, 2012, additional 50,000,000 ordinary shares were reserved for issuance under the 2005 SOP. Under the terms of the 2005 SOP, stock options are generally granted at fair market value of the Company’s ordinary shares. The stock options have a contractual term of 8 years from the date of grant and vest over a requisite service period of 4 years. As of December 31, 2016, the number of stock options outstanding and exercisable was 166,957,900 and 131,774,600, respectively, under the 2005 SOP.

In 2015, the Board adopted the 2015 Stock Incentive Plan (“2015 SIP”), which was approved by the Shareholders in July 2015, and replaced the 2005 SOP after it expired on March 2, 2016. The 2015 SIP succeeded the 2005 SOP and the 2005 Share Incentive Plan (“2005 SIP”). The 2015 SIP provides for the granting to employees of incentive stock options, restricted shares, cash dividend equivalent rights, RSUs or stock appreciation rights or similar right (collectively referred to as “Awards”) to the employees, directors and consultants of the Company. The maximum aggregate number of new shares reserved for issuance pursuant to all Awards under the 2015 SIP is 100,000,000 ordinary shares, plus the remaining balance rolled into the 2015 SIP from the 2005 SOP and 2005 SIP, respectively. The maximum number of and kind of Awards granted under the 2015 SIP shall not each exceed 125,000,000 ordinary shares. The Awards granted are generally vested over a requisite service period of 4 years. As of December 31, 2016, the number of stock options outstanding and exercisable was 40,880,000 and 6,632,700, respectively, under the 2015 SIP.

A summary of the Company’s stock option activity under the plans as of December 31, 2016, and changes during the year then ended is presented as follows:

	Number of Options Shares	Weighted Average Exercise Price	Weighted Average Remaining Contract Life	Aggregate Intrinsic Value
Outstanding Options, January 1, 2016	177,528,800	\$ 0.0869		
Granted	51,055,000	\$ 0.0310		
Exercised	(84,750)	\$ 0.0274		
Forfeited or expired	(20,661,150)	\$ 0.1273		
Outstanding Options, December 31, 2016	<u>207,837,900</u>	\$ 0.0692	<u>4.38</u>	<u>\$ 246,000</u>
Vested and Expected to Vest Options at December 31, 2016	<u>205,165,725</u>	\$ 0.0696	<u>4.35</u>	<u>\$ 229,000</u>
Exercisable Options at December 31, 2016	<u>138,407,300</u>	\$ 0.0808	<u>3.20</u>	<u>\$ 47,000</u>

The total intrinsic value of options exercised during the years ended December 31, 2016, 2015, and 2014 was \$1,000, \$2,000, and \$13,000, respectively.

The following table summarizes information about outstanding and vested stock options:

Range of Exercise Prices	Options Outstanding		Options Exercisable		
	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable and Vested	Weighted Average Exercise Price
\$0.0274 - \$0.0314	41,528,150	7.21	\$ 0.0305	8,127,950	\$ 0.0304
\$0.0338 - \$0.0472	40,817,600	2.47	\$ 0.0439	30,310,650	\$ 0.0462
\$0.0506 - \$0.0750	50,921,850	5.03	\$ 0.0625	38,091,550	\$ 0.0635
\$0.0776 - \$0.1040	33,986,400	4.98	\$ 0.0841	21,293,250	\$ 0.0865
\$0.1122 - \$0.1636	<u>40,583,900</u>	2.10	\$ 0.1301	<u>40,583,900</u>	\$ 0.1301
Balance, December 31, 2016	<u>207,837,900</u>	4.38	\$ 0.0692	<u>138,407,300</u>	\$ 0.0808

The Company calculated the fair value of each option grant on the date of grant using the Black-Scholes option pricing model that use the assumptions in the following table. Risk-free interest rate is based on the US Treasury yield curve in effect at the time of grant. The Company uses the simplified method to estimate the expected life because the options are considered as plain vanilla share-based payment awards. Expected volatilities are based on historical volatility of stock prices for a period equal to the options’ expected term. The dividend yield is zero as the Company has never declared or paid dividends on the ordinary shares or other securities and does not anticipate paying dividends in the foreseeable future.

	Stock Options			Employee Stock Purchase Plan		
	Years Ended December 31			Years Ended December 31		
	2016	2015	2014	2016	2015	2014
Risk-free interest rate	1.14% - 1.33%	1.18% - 1.50%	1.49% - 1.76%	0.22% - 0.35%	0.01% - 0.08%	0.02% - 0.05%
Expected life (Years)	5	5	5	0.25 - 0.26	0.25 - 0.26	0.25 - 0.26
Volatility	34%	33% - 36%	34% - 37%	34% - 48%	35% - 48%	30% - 45%
Dividend	-	-	-	-	-	-

The weighted-average grant-date fair value of options granted during the years ended December 31, 2016, 2015, and 2014 was \$0.0097, \$0.0127, and \$0.0245, respectively. The weighted-average fair value of options granted under the 2009 Purchase Plan during the years ended December 31, 2016, 2015, and 2014 was \$0.0054, \$0.008, and \$0.0104, respectively.

#### Share Incentive Plan

The Board adopted the 2005 SIP, which was effective on March 2, 2006, the date the Company completed the SEHK listing. The 2005 SIP provides for the grant of restricted shares, RSU, share appreciation rights and dividend equivalent rights up to 75,000,000 ordinary shares. As approved by the EGM held on May 30, 2009, the number of shares available for issue was increased from 75,000,000 to 125,000,000 shares. The references to Hong Kong and Hong Kong related rules and regulations were also removed along with the completion of the Company's delisting from the SEHK. As approved by the AGM held on June 22, 2012, an additional 62,500,000 ordinary shares were reserved for issuance under the 2005 SIP. These awards under 2005 SIP may be granted to employees, directors and consultants of the Company. The granted RSUs are generally vested over a requisite service period of 4 years. In 2015, the Board adopted the 2015 SIP, which was approved by the Shareholders in July 2015, and replaced the 2005 SIP after it expired on March 2, 2016. Please refer to above discussions for 2015 SIP.

A summary of the status of the Company's RSUs as of December 31, 2016, and changes during the year ended December 31, 2016, is presented as follows:

	Number of Outstanding RSUs	Weighted Average Grant-Date Fair Value
Nonvested at January 1, 2016	50,608,350	\$ 0.0588
Granted	34,786,850	\$ 0.0303
Vested	(18,056,150)	\$ 0.0647
Forfeited and expired	(9,401,200)	\$ 0.0441
Nonvested at December 31, 2016	<u>57,937,850</u>	\$ 0.0438

As of December 31, 2016, there was \$2,326,000 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the plans including stock options and RSUs. The cost is expected to be recognized over a weighted-average period of 2.35 years. The total fair value of RSUs vested during the years ended December 31, 2016, 2015, and 2014 was \$1,169,000, \$1,246,000, and \$1,189,000, respectively.

Cash received from option exercise under all share-based payment arrangements for the years ended December 31, 2016, 2015, and 2014, was \$75,000, \$211,000, and \$302,000, respectively.

## Ordinary Shares Reserved

As of December 31, 2016, ordinary shares reserved for future issuance were as follows:

Outstanding stock options	207,837,900
Outstanding RSUs	57,937,850
Shares reserved for future Awards grants	104,372,900
Shares reserved for Employee Stock Purchase Plan	2,620,450
	<u>372,769,100</u>

Shares issued for the exercise of stock options, Employee Stock Purchase Plan and shares vested under restricted stock units are mainly from the treasury shares.

## 16. EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per share is calculated by dividing net income (loss) by the weighted average number of ordinary shares outstanding during the period. Diluted earnings (loss) per share is calculated by dividing net income (loss) by the weighted average number of ordinary and dilutive ordinary equivalent shares outstanding during the period, using the treasury stock method for options.

A reconciliation of the numerator and denominator of basic and diluted earnings (loss) per share calculations was as follows:

	Years Ended December 31		
	2016	2015	2014
Net loss (in thousands)	\$ (2,986)	\$ (21,095)	\$ (15,057)
Weighted average shares outstanding (in thousands) – basic	1,282,141	1,301,465	1,362,465
Effect of dilutive securities:			
Options and RSUs (in thousands)	-	-	-
Weighted average shares outstanding (in thousands) – diluted	<u>1,282,141</u>	<u>1,301,465</u>	<u>1,362,465</u>
Loss per share – basic and diluted	\$ -	\$ (0.02)	\$ (0.01)

Certain outstanding options and RSUs were excluded from the computation of diluted EPS since their effect would have been anti-dilutive. The anti-dilutive stock options excluded and their associated exercise prices per share were 207,837,900 shares at \$0.0274 to \$0.1636 as of December 31, 2016, 177,528,800 shares at \$0.0454 to \$0.2176 as of December 31, 2015, and 228,666,600 shares at \$0.0460 to \$0.3462 as of December 31, 2014. The anti-dilutive RSUs excluded were 57,937,850, 50,608,350 shares, and 46,823,850 shares as of December 31, 2016, 2015, and 2014, respectively.

## 17. COMMITMENTS

### Lease Commitments

The Company leases office space and certain equipment under non-cancelable operating lease agreements that expire at various dates through December 2020. For the years ended December 31, 2016, 2015, and 2014, leasing costs charged to income in relation to these agreements were \$1,899,000, \$2,106,000, and \$2,415,000, respectively. The Company's office lease provides for periodic rental increases based on the general inflation rate.

As of December 31, 2016, future minimum lease payments under all non-cancelable operating lease agreements were as follows:

Year	(In Thousands)	
	Operating Leases	
2017	\$	1,216
2018		356
2019		202
2020		68
Total minimum lease payments	<u>\$</u>	<u>1,842</u>

Purchase obligations and commitments include payments due under various types of license, maintenance and support agreements with contractual terms from one to two years. As of December 31, 2016, those purchase commitments were as follows:

(In Thousands)

Year		
2017	\$	236
2018		39
Total	\$	<u>275</u>

## 18. CONTINGENCIES

### Legal Proceedings

The Company is involved in several litigation matters relating to its intellectual property, as detailed below. While the Company cannot make any assurances regarding the eventual resolution of these matters, the Company does not believe at this time that the final outcomes will have a material adverse effect on its consolidated results of operations or financial condition.

*O<sub>2</sub>Micro, Inc. v. Texas Instruments Japan Limited.* In November 2013, the Company filed a patent infringement suit against Texas Instruments Japan Limited (“Texas Instrument”) in the Civil Division of the Tokyo District Court. The matter was closed in August 2016 with the Court finding no infringement by the defendant on the Japanese patent in question, and the Company electing not to file an appeal.

*O<sub>2</sub>Micro (China) Co., Ltd. v. Legendsec Information Technology (Beijing) Inc., et al., Chengdu Intermediate Court, China.* The Company filed a trade secret infringement suit against Yunfeng Li, Chengdu Feitong Technology Co., Ltd. and Legendsec Information Technology (Beijing) Inc. (“Legendsec”) in Chengdu Intermediate Court on August 18, 2014, requesting the three defendants to stop the infringement actions and claim for compensatory damages. Four hearings have been held since October 2014. O<sub>2</sub>Micro (China) and Yunfeng Li reached and signed a settlement agreement on December 29, 2016 and the case has been withdrawn. The matter is now closed.

*O<sub>2</sub>Micro (China) Co., Ltd. v. Legendsec Information Technology (Beijing) Inc., Beijing Haidian District People's Court, China.* The Company filed a copyright infringement suit against Legendsec Information Technology (Beijing) Inc. in Beijing Haidian District People's Court on November 19, 2014, requesting the defendant to stop the infringement actions and claim for compensatory damages. The first hearing was held on March 16, 2015. The second hearing was held on April 22, 2015. The third hearing was held on May 19, 2015. The Court made a judgment to reject the Company’s claim on July 3, 2015. The Company appealed to Beijing Intellectual Property Court on July 14, 2015. The first hearing of the second trial was held on December 23, 2015. The Court made a final judgment to reject the Company’s appeal and sustain the original judgment on February 26, 2016. The matter is now closed.

*O<sub>2</sub>Micro (China) Co., Ltd. v. Nanjing AnalogChipTech Semiconductor Co., Ltd., et al., Nanjing Intermediate Court, China.* The Company filed a patent infringement suit against Nanjing AnalogChipTech Semiconductor Co., Ltd., and Nantong Minghui Power Tools Co., Ltd. in Nanjing Intermediate Court on October 29, 2015, requesting two defendants to stop the infringement action, destroy the infringing products and claim for compensatory damages. The first hearing was held on January 18, 2016. All parties reached and signed a settlement agreement on January 18, 2016 and this case is now closed.

*O<sub>2</sub>Micro (China) Co., Ltd. v. Nanjing AnalogChipTech Semiconductor Co, Ltd., et al., Nanjing Intermediate Court, China.* The Company filed a trade secret infringement suit against Xiaohu Tang and Nanjing AnalogChipTech Semiconductor Co., Ltd. in Nanjing Intermediate Court on October 29, 2015, requesting two defendants to stop the infringement action, destroy the infringing products and claim for compensatory damages. The first hearing was held on January 11, 2016. All parties reached and signed a settlement agreement on January 18, 2016 and this case is now closed.

The Company received \$23,000, \$0, and \$\$75,000 litigation income in relation to litigation cases in China or the United States for the years ended December 31, 2016, 2015, and 2014, respectively. The Company subsequently received \$19,000 litigation income in relation to litigation cases in China in January 2017.

The Company, as a normal course of business, is a party to litigation matters, legal proceedings, and claims. These actions may be in various jurisdictions and may involve patent protection and/or infringement. While the results of such litigations and claims cannot be predicted with certainty, the final outcome of such matters is not expected to have a material adverse effect on its consolidated financial position or results of operations. No assurance can be given, however, that these matters will be resolved without the Company becoming obligated to make payments or to pay other costs to the opposing parties, with the potential for having an adverse effect on the Company's financial position or its results of operations. No provision for any litigation has been provided as of December 31, 2016 and 2015.

## 19. FINANCIAL INSTRUMENTS

Information on the Company's financial instruments was as follows:

**(In Thousands)**

	December 31			
	2016		2015	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Assets</b>				
Cash and cash equivalents	\$ 31,332	\$ 31,332	\$ 41,199	\$ 41,199
Restricted cash	32	32	31	31
Short-term investments	21,532	21,532	11,233	11,233

The carrying amounts of cash and cash equivalents, restricted cash and short-term investments reported in the consolidated balance sheets approximate their estimated fair values.

Long-term investments are in privately-held companies where there is no readily determinable market value and are recorded using the cost method. Since they entail an unreasonable high cost to obtain verifiable fair values, fair value is not presented. The Company periodically evaluates these investments for impairment. If it is determined that an other-than-temporary decline has occurred in the carrying value, an impairment loss is recorded in the period of decline in value.

## 20. SEGMENT INFORMATION

The Company does not identify or allocate assets by operating segment, nor does the chief operating decision maker ("CODM") evaluate operating segments using discrete asset information. The Company does not have inter-segment revenue, and, accordingly, there is none to be reported. The Company does not allocate gains and losses from interest and other income, or income taxes to operating segments. The accounting policies for segment reporting are the same as for the Company as a whole.

Net sales to unaffiliated customers by geographic region are based on the customer's ship-to location and were as follows:

**(In Thousands)**

	Years Ended December 31		
	2016	2015	2014
China	\$ 46,784	\$ 45,854	\$ 55,133
Taiwan	3,009	2,274	2,022
Japan	2,535	3,759	4,490
Korea	2,257	879	288
Singapore	1,539	1,398	1,341
Other	437	677	317
	<u>\$ 56,561</u>	<u>\$ 54,841</u>	<u>\$ 63,591</u>



For the years ended December 31, 2016 and 2015, only one customer accounted for 10% or more of net sales. For the year ended December 31, 2014, two customers accounted for 10% or more of net sales. The percentage of net sales to these customers was as follows:

	<i>Years Ended December 31</i>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
Customer A	10%	11%	12%
Customer B	8%	8%	10%

Long-lived assets consisted of property and equipment and were as follows based on the physical location of the assets at the end of each year:

**(In Thousands)**

	<b>December 31</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
Taiwan	\$ 5,607	\$ 5,813	\$ 8,689
U.S.A.	4,176	4,162	4,188
China	3,920	3,997	6,363
Other	33	39	123
	<u>\$ 13,736</u>	<u>\$ 14,011</u>	<u>\$ 19,363</u>

THE COMPANIES LAW (2007 REVISION)

COMPANY LIMITED BY SHARES

AMENDED AND RESTATED

ARTICLES OF ASSOCIATION

OF

**O2MICRO INTERNATIONAL LIMITED**

(adopted pursuant to a special resolution passed on 29 May 2009)<sup>2</sup>

1 In these Articles Table A in the Schedule to the Law does not apply and, unless there be something in the subject or context inconsistent therewith,

"Articles"	means these Articles as originally framed or as from time to time altered by Special Resolution.
"Auditors"	means the persons for the time being performing the duties of auditors of the Company.
"Board"	means the board of Directors of the Company.
"Business Day"	means a day (other than a Saturday or Sunday) on which banks are open for business in California, United States and the Cayman Islands.
"Company"	means the above named O2Micro International Limited.
"debenture"	means debenture stock, mortgages, bonds and any other such securities of the Company whether constituting a charge on the assets of the Company or not.
"Designated Stock Exchange"	means a stock exchange in respect of which the shares of the Company are listed or quoted and where such stock exchange deems such listing or quotation to be the primary listing or quotation of the shares of the Company.

<sup>2</sup> The adoption of these amended and restated memorandum and articles of association was conditional upon, and took effect from, the withdrawal of the listing of the ordinary shares of the Company on the Main Board of The Stock Exchange of Hong Kong Limited on 9 September 2009.



<b>"Directors"</b>	means the directors for the time being of the Company.
<b>"dividend"</b>	includes bonus.
<b>"dollars" or "US\$"</b>	refers to the dollar currency of the United States of America and references to cents or should be construed accordingly.
<b>"Law"</b>	shall mean the Companies Law (2007 Revision) of the Cayman Islands as amended and every statutory modification or re enactment thereof for the time being in force.
<b>"Ordinary Shares"</b>	means the Ordinary Shares of nominal or par value US\$0.00002 each.
<b>"Member"</b>	shall bear the meaning ascribed to it in the Law.
<b>"month"</b>	means calendar month.
<b>"Preference Shares"</b>	means the Preference Shares of nominal or par value US\$0.00002 having the designations, powers, preferences, privileges, participating, optional or special rights, and the qualifications, limitations or restrictions thereof including, without limitation, dividend rights, voting rights, terms of redemption and liquidation preferences as the Directors shall in their sole discretion determine in accordance with these Articles.
<b>"registered office"</b>	means the registered office for the time being of the Company.
<b>"Seal"</b>	means the common seal of the Company and includes every duplicate seal.
<b>"Secretary"</b>	includes an Assistant Secretary and any person appointed to perform the duties of Secretary of the Company.
<b>"shares"</b>	shall be construed as a reference to shares of each class of share of the Company from time to time in issue and includes fractions of shares (except as otherwise provided herein).

**"Special Resolution"** has the same meaning as in the Law but does not include a resolution approved in writing as described therein.

**"written"** and **"in writing"** include all modes of representing or reproducing words in visible form.

Words importing the singular shall include the plural and vice versa.

Words importing either gender shall include the other gender and the neuter.

Words importing persons shall include corporations.

References to **"general meetings"** in these Articles shall include annual general meetings and extraordinary general meetings.

- 2 The business of the Company may be commenced as soon after incorporation as the Directors shall see fit, notwithstanding that part only of the shares may have been allotted.
- 3 The Directors may pay, out of the capital or any other monies of the Company, all expenses incurred in or about the formation and establishment of the Company including the expenses of registration.

#### ISSUE OF SHARES

- 4 At the date of adoption of these Articles of Association the Company is authorised to issue 4,750,000,000 Ordinary Shares with nominal or par value of US\$0.00002 each and 250,000,000 Preference Shares of nominal or par value of US\$0.00002 each.
- 5 Subject as herein provided and subject to any special terms of issue imposed in accordance with Article 6, the shares shall rank equally and in accordance with these Articles.
- 6 All shares in the Company for the time being unallotted and unissued shall be under the control of the Directors who may allot, issue, grant options over or otherwise dispose of shares of the Company with or without preferred, deferred or other special rights or restrictions whether in regard to dividend, voting, return of capital or otherwise and to such persons, at such times and on such other terms as they think proper.
- 7 The Company shall maintain a register of its Members and every person whose name is entered as a Member in the register of Members shall be entitled without payment to receive within two months after allotment or lodgement of transfer (or within such other period as the conditions of issue shall provide) one certificate for all his shares or several certificates each for one or more of his shares upon payment of fifty cents (US\$0.50) for every certificate after the first or such less sum as the Directors shall from time to time

determine provided that in respect of a share or shares held jointly by several persons the Company shall not be bound to issue more than one certificate and delivery of a certificate for a share to one of the several joint holders shall be sufficient delivery to all such holders.

#### **SHARE RIGHTS**

- 8 Subject to the provisions of the Law, the Memorandum of Association and Articles of Association of the Company, the rules of any Designated Stock Exchange, and to any special rights conferred on the holders of any shares or attaching to any class of shares, shares may be issued or converted into shares that, at a determinable date, or on the terms that they may be, or at the option of the Company or the holder are, liable to be redeemed on such terms and in such manner, including out of capital, as the Board may deem fit.

#### **MODIFICATION OF RIGHTS**

- 9 If at any time the share capital of the Company is divided into different classes of shares, all or any of the rights attached to any class of shares for the time being issued (unless otherwise provided for in the terms of issue of the shares of that class) may, subject to the provisions of the Law, be varied or abrogated with the consent in writing of the holders of not less than three fourths in nominal value of the issued shares of that class or with the sanction of a Special Resolution passed at a separate meeting of the holders of shares of that class. To every such separate meeting all the provisions of these Articles relating to general meetings shall mutatis mutandis apply, but so that the quorum for the purposes of any such separate meeting and of any adjournment thereof shall be a person or persons together holding (or representing by proxy) at the date of the relevant meeting not less than one-third in nominal value of the issued shares of that class, and that any holder of shares of the class present in person (or in the case of a corporation, by its duly authorized representative) or by proxy may demand a poll.
- 10 The special rights conferred upon the holders of shares of any class shall not, unless otherwise expressly provided in the rights attaching to or the terms of issue of such shares, be deemed to be varied by the creation or issue of further shares ranking pari passu therewith or in priority thereto.

#### **REDEMPTION AND REPURCHASE OF SHARES**

- 11 Subject to the Law and to any rights conferred on the holders of any class of shares, the Company shall have the power to (a) purchase or otherwise acquire all or any of its own shares (which expression as used in this Article includes redeemable shares), (b) purchase or otherwise acquire warrants for the subscription or purchase of its own shares and shares and warrants for the subscription or purchase of any shares in any company which is its holding company and (c) give, directly or indirectly, by means of a loan, a guarantee, a gift, an indemnity, the provision of security or otherwise howsoever, financial assistance for the purpose of or in connection with a purchase or other

acquisition made or to be made by any person of any shares or warrants in the Company or any company which is a holding company of the Company. The Company may pay for such shares or warrants in any manner authorised or not prohibited by law, including out of capital. Should the Company purchase or otherwise acquire its own shares or warrants, neither the Company nor the Board shall be required to select the shares or warrants to be purchased or otherwise acquired rateably or in any other manner as between the holders of shares or warrants of the same class or as between them and the holders of shares or warrants of any other class or in accordance with the rights as to dividends or capital conferred by any class of shares. Any such purchase or other acquisition or financial assistance shall only be made in accordance with any relevant code, rules or regulations issued by the Designated Stock Exchange from time to time in force for so long as the shares of the Company are listed on such Exchange.

- 12 Subject to the provisions of the Law and the Memorandum of Association of the Company and to any special rights conferred on the holders of any shares or attaching to any class of shares, shares may be issued on the terms that they may be, or at the option of the Company or the holders are, liable to be redeemed on such terms and in such manner, including out of capital, as the Board may deem fit.
- 13 The purchase or redemption of any share shall not be deemed to give rise to the purchase or redemption of any other share.
- 14 The holder of the shares being purchased, surrendered or redeemed shall be bound to deliver up to the Company at its registered office or such other place as the Board shall specify the certificate(s) thereof for cancellation and thereupon the Company shall pay to him the purchase or redemption monies in respect thereof.

#### COMMISSION ON SALE OF SHARES

- 15 The Company may in so far as the Law from time to time permits pay a commission to any person in consideration of his subscribing or agreeing to subscribe whether absolutely or conditionally for any shares of the Company. Such commissions may be satisfied by the payment of cash or the lodgement of fully or partly paid up shares or partly in one way and partly in the other. The Company may also on any issue of shares pay such brokerage as may be lawful.

#### NON RECOGNITION OF TRUSTS

- 16 No person shall be recognised by the Company as holding any share upon any trust and the Company shall not be bound by or be compelled in any way to recognise (even when having notice thereof) any equitable, contingent, future, or partial interest in any share, or any interest in any fractional part of a share, or (except only as is otherwise provided by these Articles or the Law) any other rights in respect of any share except an absolute right to the entirety thereof in the registered holder.

#### REGISTER OF MEMBERS AND SHARE CERTIFICATES

- 17 The Company shall, in accordance with the Law and the rules of the Designated Stock Exchange, cause to be kept in one or more books a register of Members, and there shall be entered therein the particulars of the members and the shares issued to each of them and other particulars required under the Law and the rules of the Designated Stock Exchange.
- 18 The register may be closed at such times and for such periods as the Board may from time to time determine, either generally or in respect of any class of shares, provided that the register shall not be closed for more than 30 days in any year (or such longer period as the members may by ordinary resolution determine provided that such period shall not be extended beyond 60 days in any year).
- 19 Every person whose name is entered as a member in the register shall be entitled without payment to receive, within 60 days, after allotment or lodgment of transfer (or within such other period as the conditions of issue shall provide), one certificate for all his shares of each class or, upon payment of such reasonable fee as the Board shall prescribe, such number of certificates for shares held as that person may request, provided that in respect of a share or shares held jointly by several persons the Company shall not be bound to issue a certificate or certificates to each such person, and the issue and delivery of a certificate or certificates to one of several joint holders shall be sufficient delivery to all such holders.
- 20 Every certificate for shares or debentures or representing any other form of security of the Company shall be issued under the seal of the Company, which shall only be affixed with the authority of the Board.
- 21 Every share certificate shall specify the number of shares in respect of which it is issued and the amount paid thereon or the fact that they are fully paid, as the case may be, and may otherwise be in such form as the Board may from time to time prescribe.
- 22 The Company shall not be bound to register more than four persons as joint holders of any share. If any share shall stand in the names of two or more persons, the person first named in the register shall be deemed the sole holder thereof as regards service of notices and, subject to the provisions of these Articles, all or any other matters connected with the Company, except the transfer of the share.
- 23 If a share certificate is defaced, lost or destroyed, it may be replaced on payment of such reasonable fee, if any, as the Board may from time to time prescribe and on such terms and conditions, if any, as to publication of notices, evidence and indemnity, as the Board thinks fit and where it is defaced or worn out, after delivery up of the old certificate to the Company for cancellation, provided always that where share warrants have been issued, no new share warrant shall be issued to replace one that has been lost unless the Directors are satisfied beyond reasonable doubt that the original has been destroyed. The fee or

fees shall not exceed the maximum fees prescribed by applicable law, rules or regulations.

#### **TRANSFER OF SHARES**

- 24 All transfers of shares may be effected by an instrument of transfer in the usual common form or in such other form as the Board may approve. All instruments of transfer must be left at the registered office of the Company or at such other place as the Board may appoint and all such instruments of transfer shall be retained by the Company.
- 25 The instrument of transfer shall be executed by or on behalf of the transferor and by or on behalf of the transferee PROVIDED that the Board may dispense with the execution of the instrument of transfer by the transferee in any case which it thinks fit in its discretion to do so. The instrument of transfer of any share shall be in writing and shall be executed with a manual signature or facsimile signature (which may be machine imprinted or otherwise) by or on behalf of the transferor and transferee PROVIDED that in the case of execution by facsimile signature by or on behalf of a transferor or transferee, the Board shall have previously been provided with a list of specimen signatures of the authorised signatories of such transferor or transferee and the Board shall be reasonably satisfied that such facsimile signature corresponds to one of those specimen signatures. The transferor shall be deemed to remain the holder of a share until the name of the transferee is entered in the register in respect thereof.
- 26 The Board may, in its absolute discretion, and without assigning any reason, refuse to register a transfer of any share which is not fully paid up or on which the Company has a lien. The Board may also decline to register any transfer of any shares unless:
- (a) the instrument of transfer is lodged with the Company accompanied by the certificate for the shares to which it relates (which shall upon registration of the transfer be cancelled) and such other evidence as the Board may reasonably require to show the right of the transferor to make the transfer and/or with regard to whether or not the transfer would result in any contravention of the restrictions (if any) on the holding of shares imposed by the Board;
  - (b) the instrument of transfer is in respect of only one class of shares;
  - (c) the instrument of transfer is properly stamped (in circumstances where stamping is required);
  - (d) in the case of a transfer to joint holders, the number of joint holders to which the share is to be transferred does not exceed four;
  - (e) the shares concerned are free of any lien in favour of the Company; and



- (f) a fee of such maximum amount as the Designated Stock Exchange may from time to time determine to be payable (or such lesser sum as the Board may from time to time require) is paid to the Company in respect thereof.
- 27 If the Board shall refuse to register a transfer of any share, it shall, within two months after the date on which the transfer was lodged with the Company, send to each of the transferor and the transferee notice of such refusal.
- 28 No transfer shall be made to an infant or to a person in respect of whom an order has been made by an competent court or official on the grounds that he is or may be suffering from mental disorder or is otherwise incapable of managing his affairs or under other legal disability.
- 29 Upon every transfer of shares the certificate held by the transferor shall be given up to be cancelled, and shall forthwith be cancelled accordingly, and a new certificate shall be issued without charge to the transferee in respect of the shares transferred to him, and if any of the shares included in the certificate so given up shall be retained by the transferor, a new certificate in respect thereof shall be issued to him without charge. The Company shall also retain the instrument(s) of transfer.
- 30 The registration of transfers may be suspended and the register closed at such times for such periods as the Board may from time to time determine, provided always that such registration shall not be suspended or the register closed for more than 30 days in any year (or such longer period as the members may by ordinary resolution determine provided that such period shall not be extended beyond 60 days in any year).

#### **COMPULSORY TRANSFER OF SHARES**

- 31 The Board shall have power to impose such restrictions as it may think necessary for the purpose of ensuring that no shares are held by:
- (a) any person in breach of the law or requirements of any country or governmental authority; or
- (b) any person or persons in circumstances (whether directly or indirectly affecting such person or persons and whether taken alone or in conjunction with any other persons, connected or not, or any other circumstances appearing to the Board to be relevant) which in the opinion of the Board might result in the Company incurring any liability to taxation or suffering any other pecuniary disadvantage which the Company might not otherwise have incurred or suffered.
- 32 If it shall come to the notice of the Board that any shares are owned directly or beneficially by any person in contravention of any such restrictions as are referred to in Article 31, the Board may give notice to such person requiring him to transfer such shares to a person who would not thereby be in contravention of any such restrictions as

aforsaid. If any person upon whom such a notice is served pursuant to this paragraph does not within thirty days after such notice transfer such shares as aforesaid or establish to the satisfaction of the Board (whose judgment shall be final and binding) that such shares are not held in contravention of any such restrictions he shall be deemed upon the expiration of such period of thirty days to have given an instrument of transfer in respect of all his shares the subject of such notice and the Directors shall be entitled to sell such shares at the best price reasonably obtainable from any other person and to appoint any person to sign on his behalf such documents as may be required for the purposes of the sale and transfer. Upon the Directors resolving to sell the shares of a member pursuant to this Article, the member shall be bound forthwith to deliver to the Company or its authorised agents the certificate(s) for such shares.

- 33 Payment of the purchase moneys payable on a purchase under this Article will be made in dollars and will be deposited by the Company with or to the order of a third party bank in the name of the Company for payment to any such person. Upon the deposit of such purchase moneys as aforesaid such person shall have no further interest in such shares or any of them or any claim against the Company in respect thereof except the right to receive the moneys so deposited (without interest).
- 34 The Company may, if required to do so by law or by any authority or by the Designated Exchange, make available to such authority or to the Designated Exchange such evidence or information which may have been furnished to or which may come into the possession of the Company as regards the identity of a holder of shares and/or the qualification of such a holder to hold or to continue to hold such shares and the Company shall not be liable to such holder for any loss occasioned by reason of such disclosure.

#### TRANSMISSION OF SHARES

- 35 In the case of the death of a member, the survivor or survivors where the deceased was a joint holder, and the legal personal representatives of the deceased where he was a sole holder, shall be the only persons recognised by the Company as having any title to his interest in the shares; but nothing herein contained shall release the estate of a deceased holder (whether sole or joint) from any liability in respect of any share solely or jointly held by him.
- 36 Any person becoming entitled to a share in consequence of the death or bankruptcy or winding-up of a member may, upon such evidence as to his title being produced as may from time to time be required by the Board and subject as hereinafter provided, either be registered himself as holder of the share or elect to have some other person nominated by him registered as the transferee thereof.
- 37 If the person so becoming entitled shall elect to be registered himself, he shall deliver or send to the Company a notice in writing signed by him stating that he so elects. If he shall elect to have his nominee registered he shall testify his election by executing in favour of his nominee a transfer of such share. All the limitations, restrictions and provisions of these Articles relating to the right to transfer and the registration of transfers of shares shall be applicable to any such notice or transfer as aforesaid as if the death or

bankruptcy or winding-up of the member had not occurred and the notice or transfer were a transfer executed by such member.

- 38 A person becoming entitled to a share by reason of the death or bankruptcy or winding-up of the holder shall be entitled to the same dividends and other advantages to which he would be entitled if he were the registered holder of the share. However, the Board may, if it thinks fit, withhold the payment of any dividend payable or other advantages in respect of such share until such person shall become the registered holder of the share or shall have effectually transferred such share, but, subject to the requirements of these Articles being met, such a person may vote at meetings.

#### LIEN

- 39 The Company shall have a first and paramount lien on every share (not being a fully paid up share) for all moneys, whether presently payable or not, called or payable at a fixed time in respect of such share; and the Company shall also have a first and paramount lien and charge on all shares (other than fully paid up shares) standing registered in the name of a member (whether solely or jointly with others) for all the debts and liabilities of such member or his estate to the Company and whether the same shall have been incurred before or after notice to the Company of any equitable or other interest of any person other than such member, and whether the period for the payment or discharge of the same shall have actually arrived or not, and notwithstanding that the same are joint debts or liabilities of such member or his estate and any other person, whether such person is a member of the Company or not.
- 40 The Company's lien (if any) on a share shall extend to all dividends and bonuses declared in respect thereof. The Board may resolve that any share shall for some specified period be exempt wholly or partially from the provisions of this Article.
- 41 The Company may sell in such manner as the Board thinks fit any shares on which the Company has a lien, but no sale shall be made unless some sum in respect of which the lien exists is presently payable or the liability or engagement in respect of which such lien exists is liable to be presently fulfilled or discharged, nor until the expiration of 14 days after a notice in writing, stating and demanding payment of the sum presently payable or specifying the liability or engagement and demanding fulfilment or discharge thereof and giving notice of intention to sell in default, shall have been given to the registered holder for the time being of the shares or the person, of which the Company has notice, entitled to the shares by reason of such holder's death, mental disorder or bankruptcy.
- 42 The net proceeds of such sale by the Company after the payment of the costs of such sale shall be applied in or towards payment or satisfaction of the debt or liability or engagement in respect whereof the lien exists, so far as the same is presently payable, and any residue shall (subject to a like lien for debts or liabilities not presently payable as existed upon the shares prior to the sale and upon surrender, if required by the Company, for cancellation of the certificate for the share sold) be paid to the holder immediately before such sale of the share. For giving effect to any such sale, the Board may authorise any person to transfer the shares sold to the purchaser thereof and may enter the

purchaser's name in the register as holder of the shares, and the purchaser shall not be bound to see to the application of the purchase money, nor shall his title to the shares be affected by any irregularity or invalidity in the proceedings in reference to the sale.

#### CALLS ON SHARES

- 43 The Board may from time to time make such calls as it may think fit upon the members in respect of any monies unpaid on the shares held by them respectively (whether on account of the nominal amount of the shares or by way of premium or otherwise) and not by the conditions of allotment thereof made payable at fixed times. A call may be made payable either in one sum or by instalments. A call may be revoked or postponed as the Board may determine.
- 44 At least 14 days' notice of any call shall be given to each member specifying the time and place of payment and to whom such payment shall be made.
- 45 Every member upon whom a call is made shall pay the amount of every call so made on him to the person and at the time or times and place or places as the Board shall specify. A person upon whom a call is made shall remain liable on such call notwithstanding the subsequent transfer of the shares in respect of which the call was made.
- 46 The joint holders of a share shall be severally as well as jointly liable for the payment of all calls and instalments due in respect of such share or other moneys due in respect thereof.
- 47 The Board may from time to time at its discretion extend the time fixed for any call, but no member shall be entitled to any such extension as a matter of grace and favour.
- 48 If the sum or any instalment payable in respect of any call is unpaid on or before the day appointed for payment thereof, the person or persons from whom the sum is due shall pay interest on the same at such rate not exceeding 15 per cent. per annum as the Board shall determine from the day appointed for the payment thereof to the time of actual payment, but the Board may waive payment of such interest wholly or in part.
- 49 No member shall be entitled to receive any dividend or bonus or to be present and vote (save as proxy for another member) at any general meeting, either personally or by proxy, or be reckoned in a quorum, or to exercise any other privilege as a member until all sums or instalments due from him to the Company in respect of any call, whether alone or jointly with any other person, together with interest and expenses (if any) shall have been paid. No amount paid up in advance of calls on any share shall for this purpose be treated as paid up on the share.
- 50 At the trial or hearing of any action or other proceedings for the recovery of any money due for any call, it shall be sufficient to prove that the name of the member sued is entered in the register as the holder, or one of the holders, of the shares in respect of which such debt accrued; that the resolution making the call is duly recorded in the minute book; and that notice of such call was duly given to the member sued, in pursuance of these Articles; and it shall not be necessary to prove the appointment of the

Directors who made such call, nor any other matters whatsoever, and the proof of the matters aforesaid shall be conclusive evidence of the debt.

- 51 Any sum which by the terms of allotment of a share is made payable upon allotment or at any fixed date, whether on account of the nominal value of the share and/or by way of premium or otherwise, shall for all purposes of these Articles be deemed to be a call duly made and payable on the date fixed for payment, and in case of non payment, all the relevant provisions of these Articles as to payment of interest and expenses, liabilities of joint holders, forfeiture and the like, shall apply as if such sum had become payable by virtue of a call duly made and notified.
- 52 The Board may, if it thinks fit, receive from any member willing to advance the same, and either in money or money's worth, all or any part of the money uncalled and unpaid or instalments payable upon any shares held by him, and upon all or any of the moneys so advanced the Company may pay interest at such rate (if any) as the Board may decide. The Board may at any time repay the amount so advanced upon giving to such member not less than one month's notice in writing of its intention in that behalf, unless before the expiration of such notice the amount so advanced shall have been called up on the shares in respect of which it was advanced. No such sum paid in advance of calls shall entitle the member paying such sum to any portion of a dividend declared in respect of any period prior to the date upon which such sum would, but for such payment, become presently payable.

#### **FORFEITURE OF SHARES**

- 53 If a member fails to pay any call or instalment of a call on the day appointed for payment thereof, the Board may, at any time during such time as any part thereof remains unpaid, without prejudice to the provisions of these Articles, serve a notice on him requiring payment of so much of the call or instalment as is unpaid, together with any interest which may have accrued and which may still accrue up to the date of actual payment.
- 54 The notice shall name a further day (not earlier than the expiration of 14 days from the date of service of the notice) on or before which, and the place where, the payment required by the notice is to be made, and shall state that in the event of non payment at or before the time and at the place appointed, the shares in respect of which the call was made or instalment is unpaid will be liable to be forfeited. The Board may accept a surrender of any share liable to be forfeited hereunder and in such case, references in these Articles to forfeiture shall include surrender.
- 55 If the requirements of any such notice as aforesaid are not complied with, any share in respect of which the notice has been given may at any time thereafter, before the payment required by the notice has been made, be forfeited by a resolution of the Board to that effect. Such forfeiture shall include all dividends and bonuses declared in respect of the forfeited share, and not actually paid before the forfeiture.
- 56 Any share so forfeited shall be deemed to be the property of the Company, and may be re-allotted sold or otherwise disposed of on such terms and in such manner as the Board

thinks fit and at any time before a re allotment, sale or disposition the forfeiture may be cancelled by the Board on such terms as it thinks fit.

- 57 A person whose shares have been forfeited shall cease to be a member in respect of the forfeited shares but shall, notwithstanding, remain liable to pay to the Company all moneys which, at the date of forfeiture, were payable by him to the Company in respect of the shares, together with (if the Board shall in its discretion so require) interest thereon from the date of forfeiture until payment at such rate not exceeding 15 per cent. per annum as the Board may prescribe, and the Board may enforce the payment thereof if it thinks fit, and without any deduction or allowance for the value of the shares forfeited, at the date of forfeiture. For the purposes of this Article any sum which, by the terms of issue of a share, is payable thereon at a fixed time which is subsequent to the date of forfeiture, whether on account of the nominal value of the share or by way of premium, shall notwithstanding that time has not yet arrived, be deemed to be payable at the date of forfeiture, and the same shall become due and payable immediately upon the forfeiture, but interest thereon shall only be payable in respect of any period between the said fixed time and the date of actual payment.
- 58 A statutory declaration in writing that the declarant is a Director or Secretary of the Company, and that a share in the Company has been duly forfeited on a date stated in the declaration, shall be conclusive evidence of the facts therein stated as against all persons claiming to be entitled to the share. The Company may receive the consideration, if any, given for the share on any re allotment, sale or disposition thereof and the Board may authorise any person to execute a letter of re allotment or transfer the share in favour of the person to whom the share is re allotted, sold or disposed of and he shall thereupon be registered as the holder of the share, and shall not be bound to see to the application of the subscription or purchase money, if any, nor shall his title to the share be affected by any irregularity or invalidity in the proceedings in reference to the forfeiture, re allotment, sale or other disposal of the share.
- 59 When any share shall have been forfeited, notice of the forfeiture shall be given to the member in whose name it stood immediately prior to the forfeiture, and an entry of the forfeiture, with the date thereof, shall forthwith be made in the register. Notwithstanding the above, no forfeiture shall be in any manner invalidated by any omission or neglect to give such notice as aforesaid.
- 60 Notwithstanding any such forfeiture as aforesaid, the Board may at any time, before any share so forfeited shall have been re-allotted, sold, or otherwise disposed of, permit the share forfeited to be redeemed upon the terms of payment of all calls and interest due upon and expenses incurred in respect of the share, and upon such further terms (if any) as it thinks fit.
- 61 The forfeiture of a share shall not prejudice the right of the Company to any call already made or instalment payable thereon.
- 62 The provisions of these Articles as to forfeiture shall apply in the case of non-payment of any sum which, by the terms of issue of a share, becomes payable at a fixed time,

whether on account of the nominal value of the share or by way of premium, as if the same had been payable by virtue of a call duly made and notified.

**AMENDMENT OF MEMORANDUM OF ASSOCIATION, CHANGE OF LOCATION  
OF REGISTERED OFFICE AND ALTERATION OF CAPITAL**

- 63 Subject to and in so far as permitted by the provisions of the Law and subject to Article 9, the Company may from time to time by ordinary resolution alter or amend its Memorandum of Association otherwise than in respect to its name and objects and may, without restricting the generality of the foregoing, by ordinary resolution:
- (a) increase the share capital by such sum to be divided into shares of such amount or without nominal or par value as the resolution shall prescribe and with such rights, priorities and privileges annexed thereto, as the Company in general meeting may determine;
  - (b) consolidate and divide all or any of its share capital into shares of larger amount than its existing shares. On any consolidation of fully paid shares and division into shares of larger amount, the Board may settle any difficulty which may arise as it thinks expedient and in particular (but without prejudice to the generality of the foregoing) may as between the holders of shares to be consolidated determine which particular shares are to be consolidated into each consolidated share, and if it shall happen that any person shall become entitled to fractions of a consolidated share or shares, such fractions may be sold by some person appointed by the Board for that purpose and the person so appointed may transfer the shares so sold to the purchaser thereof and the validity of such transfer shall not be questioned, and so that the net proceeds of such sale (after deduction of the expenses of such sale) may either be distributed among the persons who would otherwise be entitled to a fraction or fractions of a consolidated share or shares rateably in accordance with their rights and interests or may be paid to the Company for the Company's benefit;
  - (c) sub-divide its existing shares or any of them into shares of smaller amount than is fixed by the Memorandum of Association or into shares without nominal or par value and so that the resolution whereby any share is sub-divided may determine that, as between the holders of the shares resulting from such sub-division, one or more of the shares may have any such preferred or other special rights, over, or may have such deferred rights or be subject to any such restrictions as compared with the others as the Company has power to attach to unissued or new shares; or
  - (d) cancel any shares which at the date of the passing of the resolution have not been taken or agreed to be taken by any person.
- 64 All new shares created hereunder shall, except as permitted by these Articles, be subject to the same provisions with reference to the payment of calls, liens, transfer, transmission, forfeiture and otherwise as the shares in the original share capital.

- 65 Subject to the provisions of the Law, the Company may by Special Resolution change its name or alter its objects.
- 66 Subject to the provisions of the Law, the Company may by Special Resolution reduce its share capital and any capital redemption reserve fund.
- 67 Subject to the provisions of the Law, the Company may by resolution of the Directors change the location of its registered office.

#### **BORROWING POWERS**

- 68 The Board may from time to time at its discretion exercise all the powers of the Company to raise or borrow or to secure the payment of any sum or sums of money for the purposes of the Company and to mortgage or charge its undertaking, property and assets (present and future) and uncalled capital or any part thereof.
- 69 The Board may raise or secure the payment or repayment of such sum or sums in such manner and upon such terms and conditions in all respects as it thinks fit and, in particular, by the issue of debentures, debenture stock, bonds or other securities of the Company, whether outright or as collateral security for any debts, liability or obligations of the Company or of any third party.
- 70 Debentures, debenture stock, bonds and other securities may be made assignable free from any equities between the Company and the person to whom the same may be issued.
- 71 Any debentures, debenture stock, bonds or other securities may be issued at a discount, premium or otherwise and with any special privileges as to redemption, surrender, drawings, allotment of shares, attending and voting at general meetings of the Company, appointment of Directors and otherwise.
- 72 The Board shall cause a proper register to be kept, in accordance with the provisions of the Law, of all mortgages and charges specifically affecting the property of the Company and shall duly comply with the requirements of the Law in regard to the registration of mortgages and charges therein specified and otherwise.
- 73 If the Company issues debentures or debenture stock (whether as part of a series or as individual instruments) not transferable by delivery, the Board shall cause a proper register to be kept of the holders of such debentures.
- 74 Where any uncalled capital of the Company is charged, all persons taking any subsequent charge thereon shall take the same subject to such prior charge, and shall not be entitled, by notice to the Members or otherwise, to obtain priority over such prior charge.

#### **GENERAL MEETING**

- 75 The Company shall within one year of its incorporation and in each year of its existence thereafter hold a general meeting as its annual general meeting and shall specify the meeting as such in the notices calling it. The annual general meeting shall be held at such time and place as the Directors shall appoint.



- 76 At these meetings the report of the Directors (if any) shall be presented.
- 77 The Directors may whenever they think fit, proceed to convene a general meeting of the Company

**NOTICE OF GENERAL MEETINGS**

- 78 At least ten days' notice (but not more than sixty days' notice) shall be given of an annual general meeting or any other general meeting, but a general meeting may be called by shorter notice, subject to the Law, if it is so agreed:
- (e) in the case of an annual general meeting, by all the Members entitled to attend and vote thereat; and
  - (b) in the case of an extraordinary general meeting, by a majority in number of the Members having the right to attend and vote at the meeting, being a majority together holding not less than ninety five per cent. in par value of the Shares giving that right.
- 79 The accidental omission to give notice of a general meeting to, or the non receipt of notice of a meeting by, any person entitled to receive notice thereof shall not invalidate the proceedings of that meeting.
- 80 Every notice shall be exclusive of the day on which it is given or deemed to be given and of the day for which it is given and shall specify the place, the day and the hour of the meeting and the general nature of the business and shall be given in manner hereinafter mentioned or in such other manner if any as may be prescribed by the Company PROVIDED that a general meeting of the Company shall, whether or not the notice specified in this Article has been given, be deemed to have been duly convened if it is so agreed either before or after the meeting by each person entitled to vote thereat who was not present in person (or in the case of a corporation, by its duly authorized representative) or by proxy by such person signing a written waiver of notice or a consent to the holding of the meeting or an approval of the minutes thereof. The waiver of notice, consent or approval need not specify either the business to be transacted or the purpose of any general meeting except that if action is taken or proposed to be taken in relation to the waiver of notice, consent or approval shall state the general nature of the proposal. All such waivers, consents and approvals shall be filed with the corporate records of the Company or referred to in the minutes of the Meeting. Attendance by a Member at a meeting shall also constitute a waiver of notice except when that person objects at the beginning of the meeting to the transaction of any business before the meeting is not lawfully called or convened. Such notice shall state the place, date, and hour of the meeting and (a) in the case of a general meeting other than an annual general meeting, the general nature of the business to be transacted, and no other business may be transacted, or (b) in the case of the annual general meeting, those matters which the Directors, at the time of the mailing of the notice, intends to present for action by the Members, and, subject to the provisions of Articles 93 and 94 hereof, any proper matter may be presented at the meeting for such action. The notice of any meeting at which Directors

are to be elected shall include the names of nominees intended at the time of the notice to be presented by the Directors for election.

#### **PROCEEDINGS AT GENERAL MEETINGS**

- 81 No business shall be transacted at any general meeting unless a quorum of Members is present at the time when the meeting proceeds to business; the quorum shall be Members present in person (or in the case of a corporation, by its duly authorized representative) or by proxy holding a majority of shares carrying the right to vote. Members present in person (or in the case of a corporation, by its duly authorized representative) or by proxy at a meeting at which a quorum is present when the meeting proceeds to business may continue to do business until adjournment notwithstanding that a quorum ceases to exist provided any action taken is approved by at least a majority of the holders required to constitute a quorum.
- 82 If within half an hour from the time appointed for the meeting a quorum is not present, the meeting, if convened upon the requisition of Members, shall be dissolved and in any other case it shall stand adjourned to the same day in the next week at the same time and place or to such other time or such other place as the directors may determine and if at the adjourned meeting a quorum is not present within half an hour from the time appointed for the meeting the Members present shall be a quorum.
- 83 The Chairman, if any, of the Board shall preside as Chairman at every general meeting of the Company, or if there is no such Chairman, or if he shall not be present within fifteen minutes after the time appointed for the holding of the meeting, or is unwilling to act, the Directors present shall elect one of their number to be Chairman of the meeting.
- 84 If at any general meeting no Director is willing to act as Chairman or if no Director is present within fifteen minutes after the time appointed for holding the meeting, the Members present shall choose one of their number to be Chairman of the meeting.
- 85 The Chairman may, with the consent of any general meeting duly constituted hereunder, and shall if so directed by the holders, present in person (or in the case of a corporation, by its duly authorized representative) or by proxy, of a majority of the shares held by Members present at that meeting in person (or in the case of a corporation, by its duly authorized representative) or by proxy, adjourn the meeting from time to time and from place to place, but no business shall be transacted at any adjourned meeting other than the business left unfinished at the meeting from which the adjournment took place. When a general meeting is adjourned for more than forty five days or a new record date is fixed for the adjourned meeting, notice of the adjourned meeting shall be given as in the case of an original meeting; save as aforesaid it shall not be necessary to give any notice of an adjournment or of the business to be transacted at an adjourned general meeting.
- 86 At any general meeting a resolution put to the vote of the meeting shall be decided on a show of hands unless a poll is, before or on the declaration of the result of the show of hands, demanded by the Chairman or any other Member present in person (or in the case of a corporation, by its duly authorized representative) or by proxy.

- 87 At any general meeting at which directors are to be elected, a Member shall be entitled to cumulate votes (i.e., cast for any candidate a number of votes greater than the number of votes which such Member normally is entitled to cast) if the candidates' names have been placed in nomination prior to commencement of the voting and the Member has given notice prior to commencement of the voting of the Member's intention to cumulate votes. If any Member has given such notice, then every Member entitled to vote may cumulate votes for candidates in nomination either (i) by giving one candidate a number of votes equal to the number of directors to be elected multiplied by the number of votes to which the Member's shares are normally entitled to, or (ii) by distributing Member's votes on the same principle among any or all of the candidates, as the Member thinks fit. The candidates receiving the highest number of affirmative votes, up to the number of directors to be elected, shall be elected; votes against any candidate and votes withheld shall have no legal effect.
- 88 Unless a poll be so demanded a declaration by the Chairman that a resolution has on a show of hands been carried, or carried unanimously, or by a particular majority, or lost, and an entry to that effect in the Company's Minute Book containing the Minutes of the proceedings of the meeting shall be conclusive evidence of that fact without proof of the number or proportion of the votes recorded in favour of or against such resolution.
- 89 The demand for a poll may be withdrawn.
- 90 Except as provided in Article 92, if a poll is duly demanded it shall be taken in such manner as the Chairman directs and the result of the poll shall be deemed to be the resolution of the general meeting at which the poll was demanded.
- 91 In the case of an equality of votes, whether on a show of hands or on a poll, the Chairman of the general meeting at which the show of hands takes place or at which the poll is demanded, shall be entitled to a second or casting vote.
- 92 A poll demanded on the election of a Chairman or on a question of adjournment shall be taken forthwith. A poll demanded on any other question shall be taken at such time as the Chairman of the general meeting directs and any business other than that upon which a poll has been demanded or is contingent thereon may be proceeded with pending the taking of the poll.
- 93 At an annual general meeting of the Members, only such business shall be conducted as shall have been properly brought before the annual general meeting. To be properly brought before an annual general meeting, business must be specified in the notice of meeting (or any supplement thereto) given by or at the direction of the Directors, otherwise properly brought before the annual general meeting by or at the direction of the Directors or otherwise properly brought before the annual general meeting by a Member. In addition to any other applicable requirements, for business to be properly brought before an annual general meeting by a Member, the Member must have given timely notice thereof in writing to the Secretary of the Company. To be timely, a Member's notice must be delivered to or mailed and received at the principal executive offices of the Company, not less than 45 days nor more than 75 days prior to the date on which the Company first mailed its proxy materials for the previous year's annual general meeting

(or the date on which the Company mails its proxy materials for the current year if during the prior year the Company did not hold an annual general meeting or if the date of the annual general meeting was changed more than 30 days from the prior year). A Member's notice to the Secretary shall set forth as to each matter the Member proposes to bring before the annual general meeting (i) a brief description of the business desired to be brought before the annual general meeting and the reasons for conducting such business at the annual general meeting, (ii) the name and record address of the Member proposing such business, (iii) the class and number of shares of the Company which are beneficially owned by the Member, and (iv) any material interest of the Member in such business. Notwithstanding anything hereof to the contrary, no business shall be conducted at the annual meeting except in accordance with the procedures set forth in this Article 93, provided, however, that nothing in this Article 93 shall be deemed to preclude discussion by any Member of any business properly brought before the annual general meeting in accordance with said procedure. The Chairman of an annual general meeting shall, if the facts warrant, determine and declare to the meeting that business was not properly brought before the meeting in accordance with the provisions of this Article 93, and if he should so determine he shall so declare to the meeting, and any such business not properly brought before the meeting shall not be transacted. Nothing in this Article 93 shall affect the right of a Member to request inclusion of a proposal in the Company's proxy statement to the extent that such right is provided by an applicable rule of the United States Securities and Exchange Commission.

- 94 In addition to any other applicable requirements, only persons who are nominated in accordance with the following procedures shall be eligible for election as Directors. Nominations of persons for election to the Board may be made at a general meeting of the Company by any nominating committee or person appointed by the Board or by any Member entitled to vote for the election of Directors at the meeting who complies with the notice procedures set forth in this Article 94. Such nominations, other than those made by or at the direction of the Board, shall be made pursuant to timely notice in writing to the Secretary of the Company. To be timely, a Member's notice must be delivered to or mailed and received at the principal executive offices of the Company, not less than 45 days nor more than 75 days prior to the date on which the Company first mailed its proxy materials for the previous year's annual general meeting (or the date on which the Company mails its proxy materials for the current year if during the prior year the Company did not hold an annual general meeting or if the date of the annual general meeting was changed more than 30 days from the prior year). Such notice shall set forth (a) as to each person whom the Member proposes to nominate for election or re-election as a Director, (i) the name, age, business address and residence address of the person, (ii) the principal occupation or employment of the person, (iii) the class and number of shares of the Company which are beneficially owned by the person, and (iv) any other information relating to the person that is required to be disclosed in solicitations for proxies for election of Directors pursuant to Rule 14a under the United States Securities Exchange Act of 1934, as amended; and (b) as to the Member giving the notice, (i) the name and record address of the Member, and (ii) the class and number of shares of the Company which are beneficially owned by the Member. The Company may require any proposed nominee to furnish such other information as may reasonably be required by the Company to determine the eligibility of such proposed nominee to serve as a Director of

the Company. No person shall be eligible for election as a Director of the Company unless nominated in accordance with the procedures set forth herein. These provisions shall not apply to nomination of any persons entitled to be separately elected by holders of Preference Shares. The Chairman of the Meeting shall, if the facts warrant, determine and declare to such meeting that a nomination was not made in accordance with the foregoing procedure, and if he should so determine, he shall so declare to such meeting and the defective nomination shall be disregarded.

#### VOTES OF MEMBERS

- 95 Subject to any rights or restrictions for the time being attached to any class or classes of shares:
- (a) on a show of hands every Member who holds an Ordinary Share or a Preference Share who is present in person (or in the case of a corporation, by its duly authorized representative) or by proxy shall have one vote; and
  - (b) on a poll every Member present in person (or in the case of a corporation, by its duly authorized representative) or by proxy shall be entitled to one vote in respect of each Ordinary Share or Preference Share held by him.
- 96 In the case of joint holders of record the vote of the senior who tenders a vote, whether in person (or in the case of a corporation, by its duly authorized representative) or by proxy, shall be accepted to the exclusion of the votes of the other joint holders, and for this purpose seniority shall be determined by the order in which the names stand in the register of Members.
- 97 A Member of unsound mind, or in respect of whom an order has been made by any court, having jurisdiction in lunacy, may vote, whether on a show of hands or on a poll, by his committee, receiver, curator bonis, or other person in the nature of a committee, receiver or curator bonis appointed by that court, and any such committee, receiver, curator bonis or other persons may vote by proxy.
- 98 No Member shall be entitled to vote at any general meeting unless he is registered as a shareholder of the Company on the record date for such meeting nor unless all calls or other sums presently payable by him in respect of shares in the Company have been paid.
- 99 No objection shall be raised to the qualification of any voter except at the general meeting or adjourned general meeting at which the vote objected to is given or tendered and every vote not disallowed at such general meeting shall be valid for all purposes. Any such objection made in due time shall be referred to the Chairman of the general meeting whose decision shall be final and conclusive.
- 100 On a poll or on a show of hands votes may be given either personally or by proxy.

#### **RECORD DATES**

- 101 For purposes of determining the Members entitled to notice of any meeting or to vote thereat or entitled to give written consent without a meeting, the Board may fix, in advance, a record date, which shall not be more than sixty days nor less than ten days before the date of any such meeting nor more than sixty days before any such action without a meeting, and in such event only shareholders of record on the date so fixed are entitled to notice and to vote or to give consents, as the case may be, notwithstanding the registration of any transfer of any shares.
- 102 If the Board does not so fix a record date:
- (a) the record date for determining Members entitled to notice of or to vote at any general meeting shall be at the close of business on the Business Day next preceding the Day on which notice is given or, if notice is waived, at the close of Business on the Business Day next preceding the day on which the meeting is held; and
  - (b) the record date for determining Members entitled to give written consent without a meeting, (i) when no prior action by the Board has been taken, shall be the day on which the first written consent is given, or (ii) when prior action by the Board has been taken, shall be at the close of business on the day on which the Board adopts the resolution relating to that action, or the sixtieth day before the date of such other action, whichever is later.
- 103 For the purposes of determining the Members entitled to receive payment of any dividend or other distribution or allotment of any rights or the Members entitled to exercise any rights in respect of any other lawful action (other than as provided above), the Board may fix, in advance, a record date, which shall not be more than sixty days before any such action. In that case, only Members of record at the close of business on the date so fixed are entitled to receive the dividend, distribution or allotment of rights, or to exercise such rights, as the case may be, notwithstanding any transfer of any shares on the books of the Company after the record date so fixed.
- 104 If the Board does not so fix a record date, then the record date for determining Members for any such purpose shall be at the close of business on the day on which the Board adopts the applicable resolution or the sixtieth (60th) day before the date of that action, whichever is later.

#### **PROXIES**

- 105 Any Member entitled to attend and vote at a meeting of the Company shall be entitled to appoint another person as his proxy to attend and vote instead of him. A Member who is the holder of two or more shares may appoint more than one proxy to represent him and vote on his behalf at a general meeting of the Company or at a class meeting. A proxy need not be a Member. In addition, a proxy or proxies representing either a Member who is an individual or a Member which is a corporation shall be entitled to exercise the same

powers on behalf of the Member which he or they represent as such Member could exercise.

- 106 The instrument appointing a proxy shall be in writing and shall be executed under the hand of the appointor or of his attorney duly authorised in writing, or, if the appointor is a corporation under the hand of an officer or attorney duly authorised in that behalf.
- 107 The instrument appointing a proxy shall be deposited at the registered office of the Company or at such other place as is specified for that purpose in the notice convening the meeting, or in any instrument of proxy sent out by the Company:
- (a) not less than 48 hours before the time for holding the meeting or adjourned meeting at which the person named in the instrument proposes to vote; or
  - (b) in the case of a poll taken more than 48 hours after it is demanded, be deposited as aforesaid after the poll has been demanded and not less than 24 hours before the time appointed for the taking of the poll; or
  - (c) where the poll is not taken forthwith but is taken not more than 48 hours after it was demanded be delivered at the meeting at which the poll was demanded to the chairman or to the secretary or to any director;

provided that the Directors may in the notice convening the meeting, or in an instrument of proxy sent out by the Company, direct that the instrument appointing a proxy may be deposited (no later than the time for holding the meeting or adjourned meeting) at the Registered Office or at such other place as is specified for that purpose in the notice convening the meeting, or in any instrument of proxy sent out by the Company. The chairman may in any event at his discretion direct that an instrument of proxy shall be deemed to have been duly deposited. An instrument of proxy that is not deposited in the manner permitted shall be invalid.

- 108 The instrument appointing a proxy may be in any usual or common form or in such other form as the Directors may approve and may be expressed to be for a particular meeting or any adjournment thereof or generally until revoked. An instrument appointing a proxy shall be deemed to include the power to demand or join or concur in demanding a poll. A validly executed proxy which does not state that it is irrevocable shall continue in full force and effect unless (i) the person who executed the proxy revokes it prior to the time of voting by delivering a writing to the Company stating that the proxy is revoked or by executing a subsequent proxy and presenting it to the meeting or by voting in person at the meeting, or (ii) written notice of the death or incapacity of the maker of that proxy is received by the Company before the vote pursuant to which that proxy is counted; provided, however, that no proxy shall be valid after the expiration of eleven months from the date of the proxy, unless otherwise provided in the proxy.
- 109 A vote given in accordance with the terms of an instrument of proxy shall be valid notwithstanding the previous death or insanity of the principal or revocation of the proxy or of the authority under which the proxy was executed, or the transfer of the share in

respect of which the proxy is given provided that no intimation in writing of such death, insanity, revocation or transfer as aforesaid shall have been received by the Company at the registered office before the commencement of the general meeting, or adjourned meeting at which it is sought to use the proxy.

- 110 Any corporation which is a Member of record of the Company may in accordance with its articles or in the absence of such provision by resolution of its Directors or other governing body authorise such person as it thinks fit to act as its representative at any meeting of the Company or of any class of Members of the Company, and the person so authorised shall be entitled to exercise the same powers on behalf of the corporation which he represents as the corporation could exercise if it were an individual Member of record of the Company.
- 111 Shares of its own stock belonging to the Company or held by it in a fiduciary capacity shall not be voted, directly or indirectly, at any meeting and shall not be counted in determining the total number of outstanding shares at any given time.
- 112 If a clearing house (or its nominee) is a Member of the Company it may, by resolution of its directors or other governing body or by power of attorney, authorise such person or persons as it thinks fit to act as its representative or representatives at any general meeting of the Company or at any general meeting of any class of Members of the Company provided that, if more than one person is so authorised, the authorisation shall specify the number and class of shares in respect of which each such person is so authorised. A person so authorised pursuant to this provision shall be entitled to exercise the same powers on behalf of the clearing house (or its nominee) which he represents as that clearing house (or its nominee) could exercise if it were an individual Member of the Company holding the number and class of shares specified in such authorisation.

#### **INSPECTORS OF ELECTION**

- 113 Before any meeting of the Members, the Board may appoint an inspector or inspectors of election to act at the meeting or its adjournment. If no inspector of election is so appointed, then the chairman of the meeting may, and on the request of any Member or a Member's proxy shall, appoint an inspector or inspectors of election to act at the meeting. The number of inspectors shall be either one (1) or three (3). If inspectors are appointed at a meeting pursuant to the request of one (1) or more Members or their proxies, then the holders of a majority of shares or their proxies present at the meeting shall determine whether one (1) or three (3) inspectors are to be appointed. If any person appointed as inspector fails to appear or fails or refuses to act, then the chairman of the meeting may, and upon the request of any Member or a Member's proxy shall, appoint a person to fill that vacancy.
- 114 Such inspectors shall:
- (a) determine the number of shares in issue and the voting power of each, the number of shares represented at the meeting, the existence of a quorum, and the authenticity, validity, and effect of proxies;



- (b) receive votes, ballots or consents;
- (c) hear and determine all challenges and questions in any way arising in connection with the right to vote;
- (d) count and tabulate all votes or consents;
- (e) determine when the polls shall close;
- (f) determine the result; and
- (g) do any other acts that may be proper to conduct the election or vote impartially.

#### DIRECTORS

- 115 There shall be a Board consisting of not less than five or more than nine persons (exclusive of alternate Directors) PROVIDED HOWEVER that the Company may from time to time by resolution passed by the holders of a majority of shares of the Company entitled to vote increase or reduce the limits in the number of Directors. The first Directors of the Company shall be determined in writing by, or appointed by a resolution of, the subscribers of the Memorandum of Association.
- 116 At the first annual general meeting of the Company after becoming eligible to have a classified Board, the Company shall divide its Board into three classes, designated Class I, Class II, and Class III, as nearly equal in number as the then total number of directors permits. At such annual general meeting, Class I directors shall be elected for a one-year term, Class II directors for a two-year term and Class III directors for a three-year term. At each annual general meeting thereafter, successors to the class of directors whose terms expire at that annual general meeting shall be elected for a three-year term. If the number of directors is changed, any increase or decrease shall be apportioned among the classes so as to maintain the number of directors in each class as nearly equal as possible, and any additional directors of any class elected to fill a vacancy resulting from an increase in such class shall hold office for a term that shall coincide with the remaining term of that class, but in no case will a decrease in the number of directors shorten the term of any incumbent director. Notwithstanding the foregoing, whenever the holders of any one or more classes or series of Preference Shares issued by the Company shall have the right, voting separately by class or series, to elect directors at an annual or general meeting of Members, the election, term of office, filling of vacancies and other features of such directorships shall be governed by the terms of these Articles applicable thereto, and such directors so elected shall not be divided into classes pursuant to this Article 116 unless expressly provided by such terms.

#### INTERESTED DIRECTORS

- 117 Any Director may continue to be or become a director, managing director, joint managing director, deputy managing director, executive director, manager or other

officer or Member of any other company in which the Company may be interested and (unless otherwise agreed between the Company and the Director) no such Director shall be liable to account to the Company or the Members for any remuneration or other benefits received by him as a director, managing director, joint managing director, deputy managing director, executive director, manager or other officer or Member of any such other company. The Directors may exercise the voting powers conferred by the shares in any other company held or owned by the Company, or exercisable by them as directors of such other company in such manner in all respects as they think fit (including the exercise thereof in favour of any resolution appointing themselves or any of them directors, managing directors, joint managing directors, deputy managing directors, executive directors, managers or other officers of such company) and any Director may vote in favour of the exercise of such voting rights in manner aforesaid notwithstanding that he may be, or is about to be, appointed a director, managing director, joint managing director, deputy managing director, executive director, manager or other officer of such a company, and that as such he is or may become interested in the exercise of such voting rights in the manner aforesaid.

- 118 A Director may hold any other office or place of profit with the Company (except that of Auditor) in conjunction with his office of Director for such period and upon such terms as the Board may determine, and may be paid such extra remuneration therefor (whether by way of salary, commission, participation in profit or otherwise) as the Board may determine, and such extra remuneration shall be in addition to any remuneration provided for by or pursuant to any other Article.
- 119 A Director or alternate Director may act by himself or his firm in a professional capacity for the Company and he or his firm shall be entitled to remuneration for professional services as if he were not a Director or alternate Director.
- 120 A shareholding qualification for Directors may be fixed by the Company in general meeting, but unless and until so fixed no qualification shall be required.
- 121 A Director or alternate Director of the Company may be or become a Director or other Officer of or otherwise interested in any company promoted by the Company or in which the Company may be interested as shareholder or otherwise and no such Director or alternate Director shall be accountable to the Company for any remuneration or other benefits received by him as a Director or Officer of, or from his interest in, such other company.
- 122 A Director who to his knowledge is in any way, whether directly or indirectly, interested in a contract or arrangement or proposed contract or arrangement with the Company shall declare the nature of his interest at the meeting of the Board at which the question of entering into the contract or arrangement is first considered, if he knows his interest then exists, or in any other case at the first meeting of the Board after he knows that he is or has become so interested, either specifically or by way of a general notice stating that, by reason of facts specified in the notice, they are to be regarded as interested in any contracts of a specified description which may subsequently be made by the Company. No person shall be disqualified from the office of Director or alternate Director or prevented by such office from contracting with the Company, either as vendor, purchaser

or otherwise, nor shall any such contract or any contract or transaction entered into by or on behalf of the Company in which any Director or alternate Director shall be in any way interested be or be liable to be avoided, nor shall any Director or alternate Director so contracting or being so interested be liable to account to the Company for any profit realised by any such contract or transaction by reason of such Director holding office or of the fiduciary relation thereby established. A Director (or his alternate Director in his absence) shall be at liberty to vote in respect of any contract or transaction in which he is interested provided that the nature of the interest of any Director or alternate Director in any such contract or transaction shall be disclosed by him at or prior to its consideration and any vote thereon.

- 123 A general notice or disclosure to the Directors or otherwise contained in the minutes of a Meeting or a written resolution of the Directors or any committee thereof that a Director or alternate Director is a shareholder of any specified firm or company and is to be regarded as interested in any transaction with such firm or company shall be sufficient disclosure under these Articles and after such general notice it shall not be necessary to give special notice relating to any particular transaction.

#### **ALTERNATE DIRECTORS AND PROXIES FOR DIRECTORS**

- 124 A Director may at any time by notice in writing delivered to the registered office of the Company or at a meeting of the Board, appoint any person (including another Director) to be his alternate Director in his place during his absence and may in like manner at any time determine such appointment. Such appointment, unless previously approved by the Board, shall have effect only upon and subject to being so approved, provided that the Board may not withhold approval of any such appointment where the proposed appointee is a Director.
- 125 The appointment of an alternate Director shall determine on the happening of any event which, were he a Director, would cause him to vacate such office or if his appointor ceases to be a Director.
- 126 An alternate Director shall be entitled to receive and waive (in lieu of his appointor) notices of meetings of the Directors and shall be entitled to attend and vote as a Director and be counted in the quorum at any such meeting at which the Director appointing him is not personally present and generally at such meeting to perform all the functions of his appointor as a Director and for the purposes of the proceedings at such meeting the provisions of these Articles shall apply as if he (instead of his appointor) were a Director. If he shall be himself a Director or shall attend any such meeting as an alternate for more than one Director his voting rights shall be cumulative and he need not use all his votes or cast all the votes he uses in the same way. To such extent as the Board may from time to time determine in relation to any committee of the Board, the foregoing provisions of this Article shall also apply mutatis mutandis to any meeting of any such committee of which his appointor is a Member. An alternate Director shall not, save as aforesaid, have power to act as a Director nor shall he be deemed to be a Director for the purposes of these Articles.

- 127 An alternate Director shall be entitled to contract and be interested in and benefit from contracts or arrangements or transactions and to be repaid expenses and to be indemnified to the same extent mutatis mutandis as if he were a Director, but he shall not be entitled to receive from the Company in respect of his appointment as alternate Director any remuneration except only such part (if any) of the remuneration otherwise payable to his appointor as such appointor may by notice in writing to the Company from time to time direct.
- 128 In addition to the foregoing provisions of this Article, a Director may be represented at any meeting of the Board (or of any committee of the Board) by a proxy appointed by him, in which event the presence or vote of the proxy shall for all purposes be deemed to be that of the Director. A proxy need not himself be a Director and the provisions of these Articles relating to the appointment of proxies by Members shall apply mutatis mutandis to the appointment of proxies by Directors save that an instrument appointing a proxy shall not become invalid after the expiration of twelve months from its date of execution but shall remain valid for such period as the instrument shall provide or, if no such provision is made in the instrument, until revoked in writing and save also that a Director may appoint any number of proxies although only one such proxy may attend in his stead at meetings of the Board (or of any committee of the Board).

#### REMUNERATION OF DIRECTORS

- 129 The Directors shall be entitled to receive by way of remuneration for their services such sum as shall from time to time be determined by the Company in general meeting or by the Board, as the case may be, such sum (unless otherwise directed by the resolution by which it is determined) to be divided amongst the Directors in such proportions and in such manner as they may agree, or failing agreement, equally, except that in such event any Director holding office for less than the whole of the relevant period in respect of which the remuneration is paid shall only rank in such division in proportion to the time during such period for which he has held office. Such remuneration shall be in addition to any other remuneration to which a Director who holds any salaried employment or office in the Company may be entitled by reason of such employment or office.
- 130 The Board may grant special remuneration to any Director, who shall perform any special or extra services at the request of the Company. Such special remuneration may be made payable to such Director in addition to or in substitution for his ordinary remuneration as a Director, and may be made payable by way of salary, commission or participation in profits or otherwise as may be agreed.
- 131 The remuneration of an Executive Director or a Director appointed to any other office in the management of the Company shall from time to time be fixed by the Board and may be by way of salary, commission, or participation in profits or otherwise or by all or any of those modes and with such other benefits (including share option and/or pension and/or gratuity and/or other benefits on retirement) and allowances as the Board may from time to time decide. Such remuneration shall be in addition to such remuneration as the recipient may be entitled to receive as a Director.

- 132 The Directors shall be entitled to be paid all expenses, including travel expenses, reasonably incurred by them in or in connection with the performance of their duties as Directors including their expenses of travelling to and from Board meetings, committee meetings or general meetings or otherwise incurred whilst engaged on the business of the Company or in the discharge of their duties as Directors.

**POWERS AND DUTIES OF DIRECTORS**

- 133 The business of the Company shall be managed by the Directors (or a sole Director if only one is appointed) who may pay all expenses incurred in promoting, registering and setting up the Company, and may exercise all such powers of the Company as are not, from time to time by the Law, or by these Articles, or such regulations, being not inconsistent with the aforesaid, as may be prescribed by the Company in general meeting required to be exercised by the Company in general meeting PROVIDED HOWEVER that no regulations made by the Company in general meeting shall invalidate any prior act of the Directors which would have been valid if that regulation had not been made.
- 134 The Directors may from time to time and at any time by powers of attorney appoint any company, firm, person or body of persons, whether nominated directly or indirectly by the Directors, to be the attorney or attorneys of the Company for such purpose and with such powers, authorities and discretions (not exceeding those vested in or exercisable by the Directors under these Articles) and for such period and subject to such conditions as they may think fit, and any such powers of attorney may contain such provisions for the protection and convenience of persons dealing with any such attorneys as the Directors may think fit and may also authorise any such attorney to delegate all or any of the powers, authorities and discretions vested in him.
- 135 All cheques, promissory notes, drafts, bills of exchange and other negotiable instruments and all receipts for monies paid to the Company shall be signed, drawn, accepted, endorsed or otherwise executed as the case may be in such manner as the Directors shall from time to time by resolution determine.
- 136 The Directors shall cause minutes to be made in books provided for the purpose:
- (a) of all appointments of officers made by the Directors;
  - (b) of the names of the Directors (including those represented thereat by an alternate or by proxy) present at each meeting of the Directors and of any committee of the Directors;
  - (c) of all resolutions and proceedings at all meetings of the Company and of the Directors and of committees of Directors.
- 137 The Directors on behalf of the Company may pay a gratuity or pension or allowance on retirement to any Director who has held any other salaried office or place of profit with the Company or to his widow or dependants and may make contributions to any fund and pay premiums for the purchase or provision of any such gratuity, pension or allowance.

- 138 The Directors may exercise all the powers of the Company to borrow money and to mortgage or charge its undertaking, property and uncalled capital or any part thereof and to issue debentures, debenture stock and other securities whether outright or as security for any debt, liability or obligation of the Company or of any third party.

#### MANAGEMENT

- 139 The Directors may from time to time provide for the management of the affairs of the Company (including the power to vote, represent and exercise on behalf of the Company any securities of other entities held by the Company) in such manner as they shall think fit and the provisions contained in the three next following paragraphs shall be without prejudice to the general powers conferred by this paragraph.
- 140 The Directors from time to time and at any time may establish any committees, local boards or agencies for managing any of the affairs of the Company and may appoint any persons to be members of such committees or local boards or any managers or agents and may fix their remuneration.
- 141 The Directors from time to time and at any time may delegate to any such committee, local board, manager or agent any of the powers, authorities and discretions for the time being vested in the Directors (including the power to vote, represent and exercise on behalf of the Company any securities of other entities held by the Company) and may authorise the members for the time being of any such local board, or any of them to fill up any vacancies therein and to act notwithstanding vacancies and any such appointment or delegation may be made on such terms and subject to such conditions as the Directors may think fit and the Directors may at any time remove any person so appointed and may annul or vary any such delegation, but no person dealing in good faith and without notice of any such annulment or variation shall be affected thereby.
- 142 Any such delegates as aforesaid may be authorised by the Directors to sub delegate all or any of the powers, authorities, and discretions for the time being vested in them.

#### MANAGING DIRECTORS

- 143 The Directors may, from time to time, appoint one or more of their body (but not an alternate Director) to the office of Managing Director for such term and at such remuneration (whether by way of salary, or commission, or participation in profits, or partly in one way and partly in another) as they may think fit but his appointment shall be subject to determination ipso facto if he ceases from any cause to be a Director and no alternate Director appointed by him can act in his stead as a Director or Managing Director.
- 144 The Directors may entrust to and confer upon a Managing Director any of the powers exercisable by them upon such terms and conditions and with such restrictions as they may think fit and either collaterally with or to the exclusion of their own powers and may from time to time revoke, withdraw, alter or vary all or any of such powers.

PROCEEDINGS OF DIRECTORS

- 145 Except as otherwise provided by these Articles, the Directors shall meet together for the despatch of business, convening, adjourning and otherwise regulating their meetings as they think fit. Questions arising at any meeting shall be decided, resolutions shall be adopted and other action shall be taken only upon the affirmative vote of a majority of the Directors and alternate Directors present at a meeting at which there is a quorum, the vote of an alternate Director not being counted if his appointor be present at such meeting.
- 146 The President, any Vice President, the Secretary or any two Directors may at any time summon a meeting of the Directors by at least four days' notice in writing or forty eight hours oral notice to every Director and alternate Director which notice shall set forth the general nature of the business to be considered PROVIDED FURTHER if notice is given in person, by cable, telex or telecopy the same shall be deemed to have been given on the day it is delivered to the Directors or transmitting organisation as the case may be. Any oral notice given personally or by telephone may be communicated either to the director or to a person at the office of the Director who the person giving the notice has reason to believe will promptly communicate it to the Director.
- 147 Notice of a meeting need not be given to any Director (i) who signs a waiver of notice or a consent to holding the meeting or an approval of the minutes thereof, whether before or after the meeting, or (ii) who attends the meeting without protesting, prior thereto or at its commencement, the lack of notice to such Director. All such waivers, consents, and approvals shall be filed with the corporate records or made part of the minutes of the meeting. A waiver of notice need not specify the purpose of any regular or special meeting of the Board.
- 148 The quorum necessary for the transaction of the business of the Directors shall be a majority of the Directors present in person or by proxy. A meeting at which a quorum is initially present may continue to transact business notwithstanding the withdrawal of Directors, if any action taken is approved by at least a majority of the required quorum for that meeting.
- 149 For the purposes of Article 148 an alternate Director or proxy appointed by a Director shall be counted in a quorum at a meeting at which the Director appointing him is not present.
- 150 A majority of the Directors present, whether or not constituting a quorum (provided there was a quorum when the meeting started) may adjourn any meeting to another time and place). Notice of the time and place of holding an adjourned meeting need not be given unless the meeting is adjourned for more than twenty-four hours. If the meeting is adjourned for more than twenty four hours, then notice of the time and place of the adjourned meeting shall be given before the adjourned meeting takes place, in the manner specified in Article 146 to the Directors not present at the time of the adjournment.
- 151 The Directors may elect a Chairman of their Board and determine the period for which he is to hold office; but if no such Chairman is elected, or if at any meeting the Chairman is

not present within thirty minutes after the time appointed for holding the same, the Directors present may choose one of their number to be Chairman of the meeting.

- 152 The Directors may delegate any of their powers to committees consisting of such member or members of the Board (including alternate Directors in the absence of their appointors) as they think fit; any committee so formed shall in the exercise of the powers so delegated conform to any regulations that may be imposed on it by the Directors.
- 153 A committee may meet and adjourn as it thinks proper. Questions arising at any meeting shall be determined by the affirmative vote of all members present.
- 154 All acts done by any meeting of the Directors or of a committee of Directors (including any person acting as an alternate Director) shall, notwithstanding that it be afterwards discovered that there was some defect in the appointment of any Director or alternate Director, or that they or any of them were disqualified, be as valid as if every such person had been duly appointed and qualified to be a Director or alternate Director as the case may be.
- 155 Members of the Board or of any committee thereof may participate in a meeting of the Board or of such committee by means of conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other and participation in a meeting pursuant to this provision shall constitute presence in person at such meeting.
- 156 A resolution in writing (in one or more counterparts), signed by all the Directors for the time being or all the members of a committee of Directors (an alternate Director being entitled to sign such resolution on behalf of his appointor) shall be as valid and effectual as if it had been passed at a meeting of the Directors or committee as the case may be duly convened and held.

#### RESIGNATION AND VACANCIES

- 157 Any director may resign effective on giving written notice to the Board, unless the notice specifies a later time for that resignation to become effective. If the resignation of a director is effective at a future time, the Board may elect a successor to take office when the resignation becomes effective.
- 158 The Directors may appoint any person to be a Director, either to fill a vacancy or as an additional Director provided that the appointment does not cause the number of Directors to exceed any number fixed by or in accordance with the Articles as the maximum number of Directors. Each Director so elected shall hold office only until the next annual meeting of the Members and shall then be eligible for re-election.
- 159 The Members may elect a Director or Directors at any time to fill any vacancy or vacancies not filled by the Directors.
- 160 The Company may by ordinary resolution remove any Director at any time.



**PRESUMPTION OF ASSENT**

- 161 Director of the Company who is present at a meeting of the Board at which action on any Company matter is taken shall be presumed to have assented to the action taken unless his dissent shall be entered in the Minutes of the meeting or unless he shall file his written dissent from such action with the person acting as the Secretary of the meeting before the adjournment thereof or shall forward such dissent by registered mail to such person immediately after the adjournment of the meeting. Such right to dissent shall not apply to a Director who voted in favour of such action.

**SEAL**

- 162 The Seal shall only be used by the authority of the Directors or of a committee of the Directors authorised by the Directors in that behalf and every instrument to which the Seal has been affixed shall be signed by one person who shall be either a Director or the Secretary or Secretary Treasurer or some person appointed by the Directors for the purpose.

PROVIDED THAT the Company may have for use in any place or places outside the Cayman Islands, a duplicate seal or seals each of which shall be a facsimile of the Common Seal of the Company and, if the Directors so determine, with the addition on its face of the name of every place where it is to be used.

PROVIDED FURTHER THAT a Director, Secretary or other officer or representative or attorney may without further authority of the Directors affix the Seal of the Company over his signature alone to any document of the Company required to be authenticated by him under Seal or to be filed with the Registrar of Companies in the Cayman Islands or elsewhere wheresoever.

**OFFICERS**

- 163 The Company may have a President, a Secretary or Secretary Treasurer appointed by the Directors who may also from time to time appoint such other officers as they consider necessary, all for such terms, at such remuneration and to perform such duties, and subject to such provisions as to disqualification and removal as the Directors from time to time prescribe.

**DIVIDENDS**

- 164 Subject to the rights, preferences and privileges attached to any class of Shares, each Ordinary Share shall be entitled to receive such dividends at such times and from time to time as the Directors consider appropriate. No dividend shall be paid on the Ordinary Shares unless a dividend has been declared or paid on each class of Preference Shares and no dividend shall be declared on any class of Preference Shares unless dividends have been declared on all other classes of Preference Shares.
- 165 All dividends declared shall be declared payable to the holders thereof registered as such on the record date specified by the Directors at the time such dividends are declared.

- 166 The Directors may, before declaring any dividends, or distributions set aside such sums as they think proper as a reserve or reserves which shall at the discretion of the Directors, be applicable for any purpose of the Company and pending such application may, at the like discretion, be employed in the business of the Company.
- 167 No dividend or distribution shall be payable except out of the profits of the Company, realised or unrealised or out of the share premium account or as otherwise permitted by the Law.
- 168 The Directors may deduct from any dividend or distribution payable to any Member all sums of money (if any) presently payable by him to the Company on account of calls or otherwise.
- 169 The Directors may declare that any dividend or distribution be paid wholly or partly by the distribution of specific assets and in particular of paid up shares, debentures, or debenture stock of any other company or in any one or more of such ways and where any difficulty arises in regard to such distribution, the Directors may settle the same as they think expedient and in particular may issue fractional certificates and fix the value for distribution of such specific assets or any part thereof and may determine that cash payments shall be made to any Members upon the footing of the value so fixed in order to adjust the rights of all Members and may vest any such specific assets in trustees as may seem expedient to the Directors.
- 170 Any dividend, interest or other monies payable in cash in respect of shares may be paid by cheque or warrant sent through the post directed to the registered address of the holder or, in the case of joint holders, to the holder who is first named on the register of Members or to such person and to such address as such holder or joint holders may in writing direct. Every such cheque or warrant shall be made payable to the order of the person to whom it is sent. Any one of two or more joint holders may give effectual receipts for any dividends, bonuses, or other monies payable in respect of the share held by them as joint holders.
- 171 No dividend shall bear interest against the Company.

#### CAPITALISATION

- 172 The Company may upon the recommendation of the Directors by ordinary resolution authorise the Directors to capitalise any sum standing to the credit of any of the Company's reserve accounts (including share premium account and capital redemption reserve fund) or any sum standing to the credit of profit and loss account or otherwise available for distribution and to appropriate such sum to Members in the proportions in which such sum would have been divisible amongst them had the same been a distribution of profits by way of dividend and to apply such sum on their behalf in paying up in full unissued shares (not being redeemable shares) for allotment and distribution credited as fully paid up to and amongst them in the proportion aforesaid. In such event the Directors shall do all acts and things required to give effect to such capitalisation, with full power to the Directors to make such provisions as they think fit for the case of shares becoming distributable in fractions (including provisions whereby the benefit of

fractional entitlements accrue to the Company rather than to the Members concerned). The Directors may authorise any person to enter on behalf of all of the Members interested into an agreement with the Company providing for such capitalisation and matters incidental thereto and any agreement made under such authority shall be effective and binding on all concerned.

#### UNTRACEABLE SHAREHOLDERS

- 173 The Company shall be entitled to sell any shares of a Member or the shares to which a person is entitled by virtue of transmission on death or bankruptcy or operation of law if and provided that:
- (a) all cheques or warrants, not being less than three in number, for any sums payable in cash to the holder of such shares have remained uncashed for a period of 12 years;
  - (b) the Company has not during that time or before the expiry of the three month period referred to in paragraph (d) below received any indication of the whereabouts or existence of the Member or person entitled to such shares by death, bankruptcy or operation of law;
  - (c) during the 12 year period, at least three dividends in respect of the shares in question have become payable and no dividend during that period has been claimed by the Member; and
  - (d) upon expiry of the 12 year period, the Company has given notice of its intention to sell such shares to the shareholder at its address as shown in the register of members and a period of three months has elapsed since such notice and the shareholder has not responded to it.
- 174 To give effect to any sale contemplated by Article 173, the Company may appoint any person to execute as transferor an instrument of transfer of the said shares and such other documents as are necessary to effect the transfer, and such documents shall be as effective as if it had been executed by the registered holder of or person entitled by transmission to such shares and the title of the transferee shall not be affected by any irregularity or invalidity in the proceedings relating thereto. The net proceeds of sale shall belong to the Company which shall be obliged to account to the former Member or other person previously entitled as aforesaid for an amount equal to such proceeds and shall enter the name of such former Member or other person in the books of the Company as a creditor for such amount. No trust shall be created in respect of the debt, no interest shall be payable in respect of the same and the Company shall not be required to account for any money earned on the net proceeds, which may be employed in the business of the Company or invested in such investments (other than shares or other securities in or of the Company or its holding company if any) or as the Board may from time to time think fit.

**DOCUMENT DESTRUCTION**

- 175 The Company shall be entitled to destroy all instruments of transfer, probate, letters of administration, stop notices, powers of attorney, certificates of marriage or death and other documents relating to or affecting title to securities in or of the Company ("Registrable Documents") which have been registered at any time after the expiration of six years from the date of registration thereof and all dividend mandates and notifications of change of address at any time after the expiration of two years from the date of recording thereof and all share certificates which have been cancelled at any time after the expiration of one year from the date of the cancellation thereof and it shall conclusively be presumed in favour of the Company that every entry in the register if purporting to have been made on the basis of an instrument of transfer or Registrable Document so destroyed was duly and properly made and every instrument of transfer or Registrable Document so destroyed was a valid and effective instrument or document duly and properly registered and every share certificate so destroyed was a valid and effective certificate duly and properly cancelled and every other document hereinbefore mentioned so destroyed was a valid and effective document in accordance with the recorded particulars thereof in the books or records of the Company, provided always that:
- (a) the provisions aforesaid shall apply only to the destruction of a document in good faith and without express notice of the Company of any claim (regardless of the parties thereto) to which the document might be relevant;
  - (b) nothing herein contained shall be construed as imposing upon the Company any liability in respect of the destruction of any such document earlier than as aforesaid or in any other circumstances which would not attach to the Company in the absence of this Article; and
  - (c) references herein to the destruction of any document include references to the disposal thereof in any manner.

**BOOKS OF ACCOUNT**

- 176 The Directors shall cause proper books of account to be kept with respect to:
- (a) all sums of money received and expended by the Company and the matters in respect of which the receipt or expenditure takes place;
  - (b) all sales and purchases of goods by the Company;
  - (c) the assets and liabilities of the Company.
- 177 Proper books shall not be deemed to be kept if there are not kept such books of account as are necessary to give a true and fair view of the state of the Company's affairs and to explain its transactions.

- 178 The minutes and accounting books and records shall be open to inspection upon the written demand of any Member, at any reasonable time during usual business hours, for a purpose reasonably related to the Member's interests as a shareholder. The inspection may be made in person or by an agent or attorney and shall include the right to copy and make extracts. Such rights of inspection shall extend to the records of each subsidiary of the Company.
- 179 The Directors may from time to time cause to be prepared and to be laid before the Company in general meeting profit and loss accounts, balance sheets, group accounts (if any) and such other reports and accounts as may be required by law.

#### AUDIT

- 180 The Auditors shall audit the profit and loss account and balance sheet of the Company in each year and shall prepare a report thereon to be annexed thereto. Such report shall be laid before the Company at its annual general meeting in each year and shall be open to inspection by any Member. The Auditors shall at the next annual general meeting following their appointment and at any other time during their term of office, upon request of the Board or any general meeting of the Members, make a report on the accounts of the Company in general meeting during their tenure of office.
- 181 The Company shall at any annual general meeting appoint an auditor or auditors of the Company who shall hold office until the next annual general meeting. The remuneration of the Auditors shall be fixed by the Company at the annual general meeting at which they are appointed provided that in respect of any particular year the Company in general meeting may delegate the fixing of such remuneration to the Board. No person may be appointed as the, or an, Auditor, unless he is independent of the Company. The Board may before the first annual general meeting appoint an auditor or auditors of the Company who shall hold office until the first annual general meeting unless previously removed by an ordinary resolution of the Members in general meeting in which case the Members at that meeting may appoint Auditors. The Board may fill any casual vacancy in the office of Auditor but while any such vacancy continues the surviving or continuing Auditor or Auditors, if any, may act. The remuneration of any Auditor appointed by the Board under this Article may be fixed by the Board.
- 182 Every statement of accounts audited by the Auditors and presented by the Board at an annual general meeting shall after approval at such meeting be conclusive except as regards any error discovered therein within three months of the approval thereof. Whenever any such error is discovered within that period, it shall forthwith be corrected, and the statement of account amended in respect of the error shall be conclusive.

#### NOTICES

- 183 Notices shall be in writing and may be given by the Company to any Member either personally or by sending it by post, cable, telex or telecopy to him or to his address as shown in the register of Members. Notices may also be served by advertisement in appropriate newspapers in accordance with the requirements of the Designated Stock Exchange.

- 184 Where a notice is sent by post, service of the notice shall be deemed to be effected by properly addressing, pre paying and posting a letter containing the notice, and to have been effected at the expiration of sixty hours after the letter containing the same is posted as aforesaid.
- 185 Where a notice is sent by cable, telex, or telecopy, service of the notice shall be deemed to be effected by properly addressing, and sending such notice through a transmitting organisation and to have been effected on the day the same is sent as aforesaid.
- 186 A notice may be given by the Company to the joint holders of record of a share by giving the notice to the joint holder first named on the register of Members in respect of the share.
- 187 A notice may be given by the Company to the person or persons which the Company has been advised are entitled to a share or shares in consequence of the death or bankruptcy of a Member by sending it through the post as aforesaid in a pre paid letter addressed to them by name, or by the title of representatives of the deceased, or trustee of the bankrupt, or by any like description at the address supplied for that purpose by the persons claiming to be so entitled, or at the option of the Company by giving the notice in any manner in which the same might have been given if the death or bankruptcy had not occurred.
- 188 Sufficient notice of every general meeting shall be given in any manner hereinbefore authorised to:
- (a) every person shown as a Member in the register of Members as of the record date for such meeting except that in the case of joint holders the notice shall be sufficient if given to the joint holder first named in the register of Members;
  - (b) every person upon whom the ownership of a share devolves by reason of his being a legal personal representative or a trustee in bankruptcy of a Member of record where the Member of record but for his death or bankruptcy would be entitled to receive notice of the meeting; and
  - (c) no other person shall be entitled to receive notices of general meetings.

#### INFORMATION

- 189 No Member shall be entitled to require discovery of or any information in respect of any detail of the Company's trading or any matter which is or may be in the nature of a trade secret or secret process which may relate to the conduct of the business of the Company and which in the opinion of the Board would not be in the interests of the Members or the Company to communicate to the public.
- 190 The Board shall be entitled to release or disclose any information in its possession, custody or control regarding the Company or its affairs to any of its Members including,

without limitation, information contained in the register of Members and transfer books of the Company.

#### WINDING UP

- 191 If the Company shall be wound up the liquidator shall apply the assets of the Company in satisfaction of creditors' claims in such manner and order as he thinks fit. Subject to the rights, preferences and privileges of any class of shares the Liquidator shall, in relation to the assets available for distribution among the Members, distribute the same to the Members in proportion to the number of shares held.
- 192 If the Company shall be wound up, and the assets available for distribution amongst the Members as such shall be insufficient to repay the whole of the paid up capital, such assets shall be distributed so that, as nearly as may be, the losses shall be borne by the Members in proportion to the capital paid up, or which ought to have been paid up, at the commencement of the winding up on the shares held by them respectively. And if in a winding up the assets available for distribution amongst the Members shall be more than sufficient to repay the whole of the capital paid up at the commencement of the winding up, the excess shall be distributed amongst the Members in proportion to the capital paid up at the commencement of the winding up on the shares held by them respectively. This Article is to be without prejudice to the rights of the holders of shares issued upon special terms and conditions.

#### INDEMNITY

- 193 The Directors and officers for the time being of the Company and any trustee for the time being acting in relation to any of the affairs of the Company and their heirs, executors, administrators and personal representatives respectively shall be indemnified to the maximum extent permitted by law out of the assets of the Company from and against all actions, proceedings, costs, charges, losses, damages and expenses which they or any of them shall or may incur or sustain by reason of any act done or omitted in or about the execution of their duty in their respective offices or trusts, except such (if any) as they shall incur or sustain by or through their own wilful neglect or default respectively and no such Director, officer or trustee shall be answerable for the acts, receipts, neglects or defaults of any other Director, officer or trustee or for joining in any receipt for the sake of conformity or for the solvency or honesty of any banker or other persons with whom any monies or effects belonging to the Company may be lodged or deposited for safe custody or for any insufficiency of any security upon which any monies of the Company may be invested or for any other loss or damage due to any such cause as aforesaid or which may happen in or about the execution of his office or trust unless the same shall happen through the wilful neglect or default of such Director, Officer or trustee.

#### FISCAL YEAR

- 194 Unless the Directors otherwise prescribe, the financial year of the Company shall end on 31 December in each year.

**AMENDMENTS OF ARTICLES**

- 195 Subject to the Law and to Article 9, the Company may at any time and from time to time by Special Resolution alter or amend these Articles in whole or in part.

**TRANSFER BY WAY OF CONTINUATION**

- 196 If the Company is exempted as defined in the Law, it shall, subject to the provisions of the Law and with the approval of a Special Resolution, have the power to register by way of continuation as a body corporate under the laws of any jurisdiction outside the Cayman Islands and to be deregistered in the Cayman Islands.

FILED TO BE A TRUE AND CORRECT COPY

SIG.

MELANIE E. RIVERS-WOODS

Assistant Registrar

29<sup>th</sup> September, 2009



SEG/154101/16430806v9



**Significant Subsidiaries of O<sub>2</sub>Micro International Limited**

O<sub>2</sub>Micro, Inc., a California corporation

O<sub>2</sub>Micro Electronics, Inc., a Taiwanese company

O<sub>2</sub>Micro International Japan Limited, a Japanese company

O<sub>2</sub>Micro (Wuhan) Co., Ltd., a Chinese company

O<sub>2</sub>Micro (Beijing) Co., Ltd., a Chinese company

O<sub>2</sub>Micro (China) Co., Ltd., a Chinese company

O<sub>2</sub>Micro (Chengdu) Co., Ltd., a Chinese company





**O<sub>2</sub>Micro International Limited**

**CERTIFICATION**

In connection with the Annual Report of O<sub>2</sub>Micro International Limited (the “Company”) on Form 20-F for the period ended December 31, 2016, as filed with the Securities and Exchange Commission (the “Report”), each of Sterling Du, Chief Executive Officer of the Company, and Perry Kuo, Chief Financial Officer of the Company, hereby certify as of the date hereof, solely for purposes of Title 18, Chapter 63, Section 1350 of the United States Code, that to the best of his knowledge:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company at the dates and for the periods indicated.

This Certification has not been, and shall not be deemed, “filed” with the Securities and Exchange Commission.

Date: March 31, 2017

By: /s/ STERLING DU  
Sterling Du  
Chief Executive Officer

Date: March 31, 2017

By: /s/ PERRY KUO  
Perry Kuo  
Chief Financial Officer and Principal Accounting Officer

**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement Nos. 333-12670, 333-12672, 333-98425, 333-101452, 333-107975, 333-116596, 333-132251, 333-153436, 333-162489 and 333-210794 on Form S-8 of our reports dated March 31, 2017, relating to the consolidated financial statements of O<sub>2</sub>Micro International Limited and subsidiaries (the “Company”) and the effectiveness of the Company’s internal control over financial reporting, appearing in this Annual Report on Form 20-F of the Company for the year ended December 31, 2016.

/s/ Deloitte & Touche  
Taipei, Taiwan  
Republic of China

March 31, 2017

