

2017  
**ANNUAL REPORT**

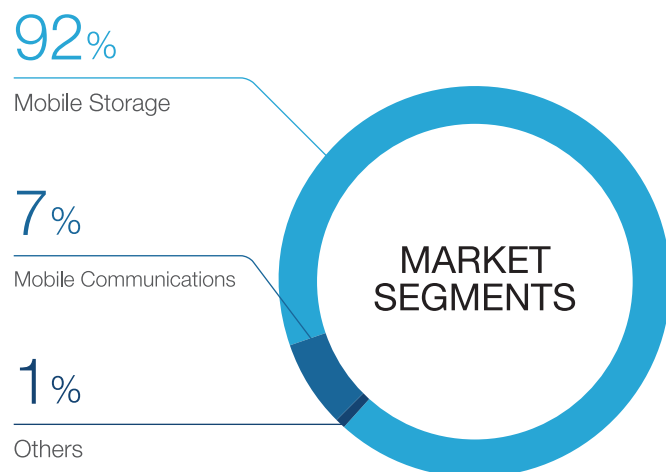


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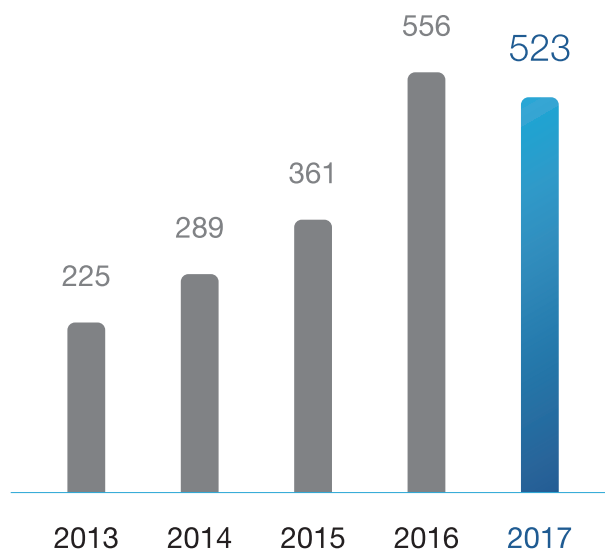
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Form 20-F  
Directors and Executives

## Financial Highlights

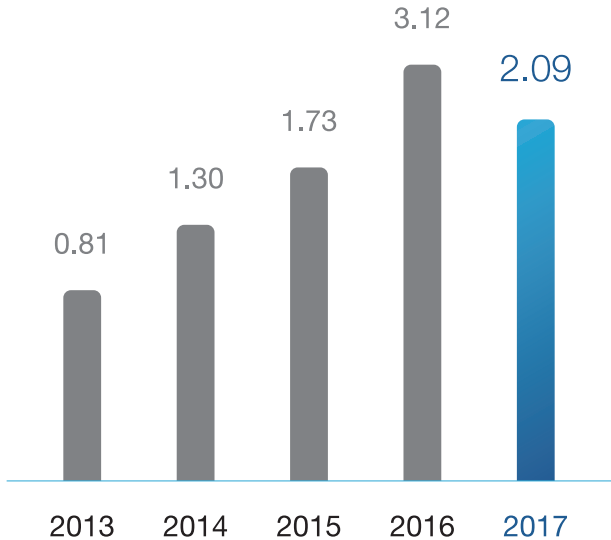
### Market Segments (% of Net Sales)



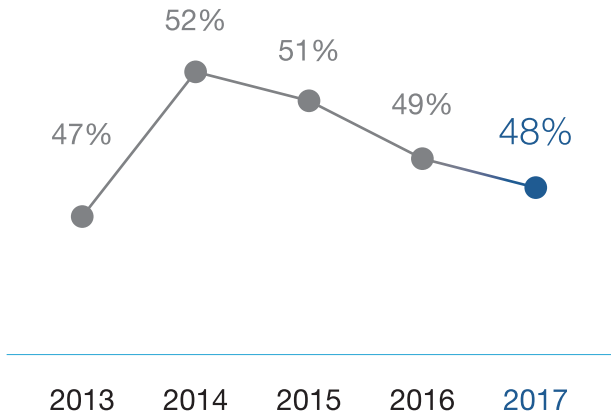
### Net Sales (US\$ millions)



**Diluted Earnings per ADS (US\$)**



**Gross Margin (% of Net Sales)**





## Letter to Shareholders

Dear Shareholders,

2017 was a challenging year for Silicon Motion as our business was affected by adverse NAND flash industry cyclicality. Revenue for the year declined 6% to \$523 million and earnings per ADS declined 23% to \$2.81 per ADS\*. In 2018, we expect NAND industry conditions to improve meaningfully as industry cyclicality reverses and our business to recover.

The NAND industry continued to be highly cyclical; this year the industry experienced supply shortages and rising prices. These two issues were especially severe in the first half of 2017. Tight supply of NAND limited our ability to build more Shannon and Ferri SSD solutions. More critically, tight supply also drove up the price of NAND and this in turn affected the affordability of client SSDs relative to HDDs and reduced demand for SSD controllers. By the second half of the year however, the NAND industry was no longer experiencing a shortage as NAND manufacturers had increased supply from the ramp of new 3D NAND capacity and sales of our SSD solutions rebounded. After several quarters of rising NAND prices, NAND prices had started to soften in the fourth quarter and sales of our client SSD controllers began to recover. In 2018, we expect NAND supply to continue improving, price of NAND to fall meaningfully and our SSD controller sales to rebound strongly.

Key 2017 business milestones include:

- Micron UFS mobile embedded memory using our controller secured first design-win with a leading global handset OEM
- Began shipping our SATA3 SSD controller to Intel for the world's first 64-layer 3D TLC NAND-based SSD, the Intel 545s
- Began shipping our SATA3 SSD controller for Micron's Crucial BX300 SSD and MX500 SSD
- Began commercial sales of our 2nd generation PCIe NVMe client SSD controllers, including to Intel for its 760p SSD
- Delivered pre-production samples of our Open-Channel NVMe SSD controller to a large Chinese hyperscale customer for its data center SSDs

In 2017, our client SSD controller sales declined a little over 10% and accounted for almost one-third of our total sales. Sales declined sequentially for three consecutive quarters and rebounded in the fourth quarter, with growth led by sales to our NAND partners. We expect our SSD controller sales growth to continue through 2018 as NAND prices are expected to fall further and our NAND partners and module maker customers plan to build more client SSDs to support PC OEMs' renewed interest in replacing HDDs with SSDs. We are very well positioned to benefit from this accelerating SSD adoption and have already secured a significant majority of client SSD projects, which have been

awarded by NAND vendors to merchant controller suppliers, because of our unique competitive advantage in providing customers with customizable hardware plus firmware controller platforms as well as complete turnkey solutions.

Our eMMC and UFS controller sales declined approximately 5% in 2017 and accounted for almost a third of total sales. eMMC and UFS controllers are primarily used in mobile embedded memory for smartphones, and since the market for smartphones is now mature and ex-growth, demand for eMMC and UFS controllers are correspondingly also ex-growth. For the foreseeable future, we aim to manage our eMMC and UFS controller sales as a stable revenue stream with declining sales of legacy eMMC controllers offset by growing sales of new UFS controllers.

Sales of our customized Ferri industrial and Shannon data center SSD solutions increased over 15% and accounted for almost 20% of total sales. In the first half of 2017, sales of our SSD solutions were affected by the NAND supply shortage; by mid-year, sales of our SSD solutions had rebounded as supply became increasingly available, despite the continuing high cost of NAND. We expect our SSD solutions sales to continue growing in 2018 as industrial and data center storage spending grow further.

Despite headwinds in 2017 from the temporary NAND supply shortage and elevated NAND prices, we remain focused on managing our business in anticipation of rapidly increasing use of NAND flash and related controllers in consumer, commercial, industrial and data center applications. Today, more than 60% of PC and other client devices are still using client HDDs, and as NAND becomes more affordable, SSDs with our controllers will quickly displace HDDs in many of these applications. Separately, we are beginning to enter the large and blue-sky enterprise and data center SSD controller market and have already started testing our new Open-Channel NVMe SSD controller with a large Chinese hyperscale customer. We will also continue to selectively leverage our unique controller technology to provide SSD solutions for enterprise, industrial and commercial applications underserved by NAND manufacturers to expand the overall addressable market for NAND.

Finally, and as always, we remain grateful to our customers for their business and trust, to our employees for their dedication and hard work and to our shareholders for their encouragement and support.

Sincerely,



James Chow  
Chairman of the Board



Wallace C. Kou  
President and Chief Executive Officer

\* Please refer to our 6-K disclosures for a reconciliation of GAAP to Non-GAAP earnings.

## About Silicon Motion

Silicon Motion is the global leader in developing NAND flash controllers for SSDs and other solid state storage devices. We have over 20 years of experience developing controllers, specialized processors that manage NAND components and deliver market leading, high-performance storage solutions widely used in smartphones, PCs, data centers and commercial and industrial applications. We have one of the broadest portfolios of controller intellectual properties developed from our deep understanding of NAND characteristics, which enables us to design both unique, highly optimized configurable IC plus related firmware controller platforms and complete turnkey controller solutions. In the last ten years, we have shipped over five billion controllers, more than any other company in the world. More NAND flash components, including 64-, 72- and 96-layer 3D TLC and QLC flash produced by Intel, Micron, Samsung, SK Hynix, Toshiba and Western Digital, are supported by Silicon Motion controllers than any other company. Our customers include most of the NAND flash makers, storage device module makers, hyperscalers and other OEMs.

We are the world's leading merchant supplier of SSD controllers used in PCs and other client devices and leading merchant supplier of eMMC/UFS controllers used in smartphones and IoT devices.

We also leverage our controller expertise to supply customized high-capacity specialty SSD solutions for the Chinese hyperscale data center market and small single-chip form-factor SSDs for high-performance industrial, commercial and automotive applications.

We market our controllers under the "SMI" brand, enterprise-grade SSDs under the "Shannon Systems" brand and single-chip industrial-grade SSDs under the "Ferri SSD" and "Ferri-eMMC" brands.

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 20-F**

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (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, 2017  
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: N/A  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number: 000-51380

**Silicon Motion Technology Corporation**

(Exact name of Registrant as specified in its charter)

Cayman Islands  
(Jurisdiction of incorporation or organization)  
Unit 04-05, 27/F, #909 Cheung Sha Wan Rd.  
Cheung Sha Wan, Kowloon  
Hong Kong  
Tel: +852 2307 4768  
Fax: + 852 2307 4368  
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:	Name of each exchange on which registered
Title of each class	
Ordinary shares, par value US\$0.01 per share* American Depositary Shares, each representing four ordinary shares	Nasdaq Global Select Market

\* Not for trading, but only in connection with the listing on the Nasdaq Global Select Market of American Depositary Shares, or ADSs, each representing four ordinary shares.

Securities registered or to be registered pursuant to Section 12(g) of the Act:  
None

Securities registered or to be registered pursuant to Section 15(d) of the Act:  
None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 143,162,340 ordinary shares as of December 31, 2017, US\$0.01 par value per share.

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 Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Emerging growth company	<input type="checkbox"/>

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards† provided pursuant to Section 13(a) of the Exchange Act.

† The term "new or revised financial accounting standard" refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012. Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP <input checked="" type="checkbox"/>	International Financial Reporting Standards as issued by the International Accounting Standards Board <input type="checkbox"/>	Other <input type="checkbox"/>
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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 Act): Yes  No

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## CONVENTIONS THAT APPLY TO THIS ANNUAL REPORT

Unless otherwise indicated, references in this annual report to:

- “ADRs” are to the American depositary receipts that evidence our ADSs;
- “ADSs” are to our American depositary shares, each of which represents four of our ordinary shares;
- “CAGR” are to compound annual growth rate;
- “China” or “PRC” are to the People’s Republic of China, excluding the special administrative regions of Hong Kong and Macau;
- “Korea” are to the Republic of Korea, or South Korea;
- “Korea Won” are to the legal currency of South Korea;
- “Nasdaq” are to the Nasdaq Stock Market;
- “NT dollar,” “NT dollars” or “NT\$” are to New Taiwan dollars, the legal currency of Taiwan;
- “ROC” or “Taiwan” are to the Republic of China, the official name of Taiwan;
- “shares” or “ordinary shares” are to our ordinary shares, with a par value US\$0.01 per share;
- “U.S. GAAP” are to generally accepted accounting principles in the United States;
- “U.S. dollar,” “U.S. dollars” or “US\$” are to United States dollars, the legal currency of the United States; and
- “we,” “us,” “our company,” “our,” “SMTC” and “Silicon Motion” are to Silicon Motion Technology Corporation, its predecessor entities and subsidiaries including but not limited to (i) Silicon Motion Technology (HK) Ltd., incorporated in Hong Kong, (ii) Silicon Motion, Inc., incorporated in Taiwan, or SMI Taiwan, and formerly known as Feiya Technology Corporation, (iii) Silicon Motion, Inc., a California, USA, corporation, or SMI USA, (iv) FCI Inc., incorporated in Korea, or FCI, and (v) Shanghai Baocun Information Technology Co., Ltd., incorporated in the PRC, or Shannon Systems.

Silicon Motion, the Silicon Motion logo, FCI, the FCI logo, the Shannon Systems logo, PCIe-RAID, DIRECT-IO, Hyper-IO, airRF, basicRF, ezRF, ezSYS, powerRF, twinRF, zipRF, zipSYS, VirtualZero, SSDLifeGuard, SSDLifeSaver, TurboMLC, FerriSSD, Ferri-eMMC, Bigtera, the Bigtera logo, the CAT logo, and NANDXtend are our trademarks or registered trademarks. We may also refer to trademarks of other corporations and organizations in this document.

Unless otherwise indicated, our financial information presented in this annual report has been prepared in accordance with U.S. GAAP.

## SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This annual report contains forward-looking statements. These forward-looking statements include statements regarding our financial position; our expectations concerning future operations, margins, profitability, liquidity and capital resources; our business strategy and other plans and objectives for future operations; and all other statements that are not historical facts. In some cases, you can identify forward-looking statements by terminology such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “thinks,” “estimates,” “seeks,” “predicts,” “potential,” and similar expressions. Although we believe that these statements are based on reasonable assumptions, they are subject to numerous factors, risks and uncertainties that could cause actual outcomes and results to be materially different from those projected. These factors, risks and uncertainties include those listed under “Risk Factors” and elsewhere in this annual report. Those factors, among others, could cause our actual results and performance to differ materially from the results and performance projected in, or implied by, the forward-looking statements. They include:

- unpredictable volume and timing of customer orders, which are not fixed by contract but vary on a purchase order basis;
- the loss of one or more key customers or the significant reduction, postponement, rescheduling or cancellation of orders from these customers;
- general economic conditions or conditions in the semiconductor or consumer electronics market;
- decreases in the overall average selling prices of our products;
- changes in the relative sales mix of our products;
- the payment, or non-payment, of cash dividends in the future at the discretion of our board of directors;
- changes in our cost of finished goods;
- the availability, pricing and timeliness of delivery of other components and raw materials used in our and our customers’ products;
- our customers’ financial health, sales outlook, purchasing patterns and inventory adjustments based on consumer demand, market adoption of new technologies and general economic conditions;
- our ability to successfully develop, introduce and sell innovative, new or enhanced products in a timely manner; and
- the timing of new product announcements or introductions by us or by our competitors.

One or more of these factors could materially and adversely affect our operating results and financial condition in future periods. We cannot assure you that we will attain any meaningful estimates or maintain profitability or that the assumptions on which they are based are reliable.

Except as required by law, we undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise after the date of this annual report. All forward-looking statements contained in this annual report are qualified by reference to this cautionary statement. As you read and consider this annual report, you should carefully understand that the forward-looking statements are not guarantees of performance or results.

## PART I

### ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

### ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

### ITEM 3. KEY INFORMATION

#### Selected Consolidated Financial Data

You should read the following information with our consolidated financial statements and related notes and “Item 5. Operating and Financial Review and Prospects” included elsewhere in this annual report.

The selected consolidated statements of income and cash flow data for the years ended December 31, 2015, 2016 and 2017 and the selected consolidated balance sheet data as of December 31, 2016 and 2017 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 and related notes. The selected consolidated statements of income for the years ended December 31, 2013 and 2014 and the selected consolidated balance sheet data as of December 31, 2013, 2014 and 2015 are derived from our audited consolidated financial statements which are not included in this annual report. To reflect our early adoption of the new accounting update on the statement of cash flows, we retrospectively adjusted the selected consolidated statements of cash flow data for the years ended December 31, 2013 and 2014, which are not derived from our audited consolidated financial statements included in our prior annual reports. These consolidated financial statements are prepared in accordance with U.S. GAAP.

	Year Ended December 31,				
	2013	2014	2015	2016	2017
	US\$	US\$	US\$	US\$	US\$
	(in thousands, except for per share data)				
<b>Consolidated Statements of Income Data:</b>					
Net sales	225,308	289,323	361,297	556,146	523,404
Cost of sales	118,698	139,625	176,765	281,541	272,210
Gross profit	106,610	149,698	184,532	274,605	251,194
Operating expenses:					
Research and development	46,460	60,949	71,161	92,405	102,053
Sales and marketing	13,597	16,324	20,173	25,765	25,868
General and administrative	11,250	13,355	15,714	17,072	16,933
Amortization of intangible assets	—	—	1,051	2,103	2,534
Impairment of goodwill	—	—	—	—	10,337
Gain from disposal of noncurrent assets held for sale	—	—	—	—	(1,880)
Total operating expenses	71,307	90,628	108,099	137,345	155,845
Operating income	35,303	59,070	76,433	137,260	95,349
Total non-operating income	1,845	1,498	2,067	1,370	3,652
Income before income taxes	37,148	60,568	78,500	138,630	99,001
Income tax expense	9,772	16,101	18,249	27,690	24,046
Net income	27,376	44,467	60,251	110,940	74,955
Weighted average shares outstanding:					
Basic	132,259	134,604	138,100	140,919	142,738
Diluted	134,567	136,787	139,634	142,050	143,606
Earnings per share:					
Basic	0.21	0.33	0.44	0.79	0.53
Diluted	0.20	0.33	0.43	0.78	0.52
Earnings per ADS <sup>(1)</sup> :					
Basic	0.83	1.32	1.75	3.15	2.10
Diluted	0.81	1.30	1.73	3.12	2.09

(1) Each ADS represents four ordinary shares.

	As of December 31,				
	2013	2014	2015	2016	2017
	US\$	US\$	US\$	US\$	US\$
	(in thousands)				
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents . . . . .	161,720	194,211	180,519	274,483	359,453
Other current assets . . . . .	83,541	96,229	134,657	202,417	209,344
Working capital . . . . .	204,594	234,374	226,889	330,914	391,553
Long-term investments . . . . .	133	133	133	120	—
Property and equipment, net . . . . .	30,195	35,537	50,469	47,892	51,370
Goodwill and intangible assets, net . . . . .	35,474	35,467	75,990	73,883	66,393
Other non-current assets . . . . .	5,700	4,957	3,860	7,231	7,172
Total assets . . . . .	316,763	366,534	445,628	606,026	693,732
Total liabilities . . . . .	46,066	62,434	101,130	163,263	199,681
Total shareholders' equity . . . . .	270,697	304,100	344,498	442,763	494,051

	As of December 31,				
	2013	2014	2015	2016	2017
	As Adjusted US\$	As Adjusted US\$	As Adjusted US\$	US\$	US\$
	(in thousands)				
<b>Consolidated Cash Flow Data:</b>					
Net cash provided by operating activities . . . . .	49,128	68,725	65,946	125,568	103,881
Net cash used in investing activities <sup>(1)</sup> . . . . .	(12,726)	(11,596)	(58,458)	(8,220)	(14,548)
Net cash provided by (used in) financing activities . . . . .	(29,493)	(19,710)	(20,271)	2,194	(31,740)
Depreciation and amortization . . . . .	6,429	6,917	8,987	11,585	13,133
Capital expenditures . . . . .	(12,772)	(11,596)	(23,664)	(12,220)	(11,683)

(1) The selected consolidated statements of cash flow data for the years ended December 31, 2013, 2014 and 2015 were retrospectively adjusted to reflect the Company's election to early adopt the accounting update of the classification and presentation of changes in restricted cash on the statement of cash flows. See Note 2 to our audited consolidated financial statement included in this annual report for more information.

## Risk Factors

*Because our operating results for any period could be adversely affected by a number of factors and may therefore fluctuate significantly, our annual and quarterly operating results are difficult to predict.*

Our operating results have fluctuated in the past and could do so in the future. For example, our net income increased \$50,689 thousand from 2015 to 2016 and decreased \$35,985 thousand from 2016 to 2017. Fluctuations in our operating results may be due to a number of factors, including, but not limited to, those listed below and those identified throughout this "Risk Factors" section:

- competitive pressures and other factors such as the qualification, availability and pricing of competing products and technologies and the resulting effects on sales and pricing of our products;
- changes in demand for electronic devices into which our semiconductor solutions are directly or indirectly incorporated;
- our customers' sales outlook, purchasing patterns and inventory adjustments based on market demand, adoption of new technologies and general economic conditions;
- the loss of one or more key customers or the significant reduction, timing or cancellation of orders from these customers;



- seasonality or cyclical fluctuations in our markets;
- our ability to develop or acquire, introduce, market and transition to volume production new or enhanced products and technologies in a cost-effective and timely manner;
- changes in supply and availability of flash memory components used in our and our customer's products;
- changes in our product mix or customer mix and their effect on our gross margin;
- changes in foreign currency exchange rates;
- the availability and pricing of third party semiconductor foundry services;
- unpredictable volume and timing of customer orders, which are not fixed by contract but vary on an order-to-order basis;
- deferrals or reductions of customer orders in anticipation of new products or product enhancements from us or our competitors or other providers of integrated circuits;
- our ability to timely and accurately predict market requirements and evolving industry trends and to identify and capitalize upon opportunities in new markets; and
- the overall cyclical nature of, and changing economic and market conditions in, the semiconductor industry.

These and other factors make it difficult for us to assess our future performance. Our sales and operating results are difficult to predict and have in the past, and will likely in the future, fluctuate from period to period. We could fail to achieve the operating targets that we have announced, such as revenue growth, gross margin, and operating expense. In addition, our operating results in the future may be below the expectations of securities analysts or investors, which would likely cause the market price of our ADSs to decline. Any variations in our period-to-period performance may also cause the market price of our ADSs to fluctuate. Accordingly, you should not rely on the results of any prior periods as a reliable indicator of our future operating performance.

***Our operating results and stock price may be adversely affected by worldwide economic uncertainties including political and social instability and industry-specific conditions in the markets we operate.***

Disruptions or uncertainties in the economy, including any political and social instability may lead consumers and business to postpone spending. This in turn may cause our customers to cancel, decrease or delay their existing and future orders with us. Furthermore, we operate primarily in the semiconductor industry, which is cyclical in nature and subject to evolving industry standards. In the past, the semiconductor industry had experienced significant downturns characterized by decreases in product demand, excess customer inventories and accelerated erosion of prices. The semiconductor industry also periodically experiences increased demand and production capacity constraints, which may affect our ability to deliver products to our customers. Economic volatility can cause extreme difficulties for our customers and vendors in accurately forecasting and planning future business activities. This unpredictability could cause our customers to reduce spending on our products and services, which would delay and lengthen sales cycles. The accurate forecasting and planning for our operations heavily rely on these worldwide economic and industry-specific conditions, and the volatility and uncertainties associated with these factors may adversely affect our results of operation in a material manner.

***Since we have limited visibility as to the sales volume by our customers of devices using our products, our ability to accurately forecast future demand for and sales of our products is limited.***

The majority of our products are integrated into devices that are sold directly or indirectly into markets which are difficult for us and our customers to accurately forecast as computing and mobile devices demand is subject to significant seasonality, with higher net sales generally in the second half of each year, when our customers place orders to meet increased demand during year-end holiday seasons, and other fluctuations. Also, as a significant portion of our quarterly sales are from orders received and fulfilled in that quarter, our visibility

as to expected orders from our customers in subsequent periods and for any extended period of time is limited. Additionally, we depend upon our customers' procurement forecasts in order to forecast demand for our products, and our customers' procurement forecast may be subject to change. Our failure to accurately forecast demand for our products may result in lost sales or excess inventory and associated reserves or write-downs for our operations. Any of the aforementioned factors could affect sales of our products and thereby harm our business, financial condition and operating results.

***If demand for our products declines in the major end-markets that we serve, our sales, net revenue and earnings will decrease.***

Demand for our products is affected by a number of factors, including the general demand for the products in the end-markets that we serve and price attractiveness of the devices incorporating our products that our customers and vendors offer to end-markets. A significant amount of our sales revenue is derived from customers who use our controllers in expandable and embedded solid state storage solutions used in computing and mobile devices. Any significant decrease in the demand for these devices in the end-market may decrease the demand for our semiconductor solutions and may result in a significant decrease in our revenues and earnings. Computing and mobile devices that use our components rapidly change as product capabilities are upgraded or new classes of products are introduced, and these changes may result in a significant reduction in demand for our products. We cannot give any assurance that there will not be any downturn in the future or that any future downturn will not affect our results of operations. Any significant decrease in demand for end-user applications of semiconductors will negatively affect our sales, net revenue and earnings.

***We may make acquisitions that are dilutive to existing shareholders, resulting in unanticipated one-time charges or that may otherwise adversely affect our results of operations, and which may result in difficulties in assimilating and integrating the operations, personnel, technologies, products and information systems of acquired companies or businesses.***

We continually evaluate and explore strategic opportunities as they arise, including acquisitions. If we issue equity securities in connection with an acquisition, the issuance may be dilutive to our existing shareholders. Alternatively, acquisitions made entirely or partially for cash would reduce our cash reserves.

Mergers and acquisitions of high-technology companies are inherently risky and subject to many factors outside of our control and no assurance can be given that our previous or future acquisitions will be successful and will not materially adversely affect our business, operating results, or financial condition. Failure to manage and successfully integrate acquisitions could materially harm our business and operating results. Even when an acquired company has already developed and marketed products, there can be no assurance that such products will be successful after our acquisition, will not cannibalize sales of our existing products, that product enhancements will be made in a timely fashion or that pre-acquisition due diligence will have identified all possible issues.

In April 2007 we completed the acquisition of FCI, a privately-held Korea-based fabless IC company focused on mobile TV and wireless communications radio frequency, or RF, applications; in November 2007, we acquired select parts of the Centronix mobile TV business of Korea Information Engineering Services Co., Ltd. ("Centronix") and in October 2011 we acquired select assets of BTL Systems, Inc. ("BTL"). The products from our FCI, Centronix and BTL acquisitions are for the mobile communications market. In the fourth quarter of 2009 and 2017, we determined that goodwill and certain long-lived assets relating to these products were impaired and recorded the impairment charge of US\$37.4 million and US\$10.3 million respectively. In July 2015 we completed the acquisition of Shannon Systems, a privately-held China-based supplier of enterprise-class PCIe SSD solutions to China's internet and other industries. In July 2017 we completed the acquisition of Bigtera, a software defined storage company.

See “*We are exposed to potential impairment charges on intangible assets relating to recent acquisitions and on investments if business conditions deteriorate*” below. Risks arising from these or other future acquisitions could include among other things:

- our ability to accurately assess the business and prospects of an acquisition or the anticipated benefits of an acquisition;
- delays in or failure to complete the development and application of the acquired technologies or products;
- timing of the rollout and adoption of new applications and technology standards;
- our ability to successfully integrate acquired technologies, operations and personnel;
- failure to achieve projected results of an acquisition or inability to realize the anticipated benefits of an acquisition;
- disruption of our ongoing business;
- diversion of management and employees’ attention from other business activities;
- risks associated with entering into a geographic region or business market in which we have little or no prior experience and specifically managing personnel in these regions;
- difficulties in establishing and maintaining uniform standards, controls, policies and procedures;
- deficiencies in the internal control of any acquired company resulting in a material weakness in our overall internal control;
- our ability to recover costs of the acquisition or investment;
- amortization expenses and large and immediate write-offs;
- impairment charges related to goodwill or other assets;
- negative impact on our relationships with customers, vendors, suppliers or contractors;
- inability to retain key employees of an acquired business; and
- potentially dilutive issuance of equity securities.

In addition, future acquisitions could result in the incurrence of debt or contingent liabilities, adverse tax consequences, deferred compensation charges, dilution to future earnings, and large fees for professional advisor services, any of which could negatively impact our financial conditions or results of operations and could cause our stock price to decline. We may be unable to identify suitable acquisition candidates or consummate any such transactions on terms and conditions that are acceptable to us, if at all.

In the future, in addition to pursuing acquisitions, we also may choose to divest business units or technologies we own or have acquired should such a divestiture make strong business sense to our board of directors and management. Such a divestment transaction can present risks of its own including successfully transitioning of the business to a third party buyer, diversion of management and employees’ attention from other business activities, and potential impairment or write-off charges necessitated by such a divestiture.

***We depend on a small number of customers for a significant portion of our revenues and a loss of some of these customers would result in the loss of a significant portion of our revenues.***

We derived a substantial portion of our revenue from sales to a relatively small number of customers. As a result, the loss of any significant customer could materially and adversely affect our financial condition and results of operations. Sales to our five largest customers represented approximately 54%, 58% and 57% of our net revenue in 2015, 2016 and 2017, respectively. Sales to two customers in 2017, and one customer in 2015 and

2016 accounted for 10% or more of our net revenue, representing 30%, 28% and 39% of our net revenue in 2015, 2016 and 2017, respectively. In 2017, the significant customers were SK Hynix and Intel and in 2015 and 2016, SK Hynix. The identities of our largest customers and their respective contributions to our net revenue have varied and will likely continue to vary from period to period.

We expect that we will continue to depend on a relatively limited number of customers for a substantial portion of our net sales and our ability to maintain good relationships with these customers will be important to the ongoing success of our business. We cannot assure you that the revenue generated from these customers, individually or in the aggregate, will reach or exceed historical levels in any future period. Our failure to meet the demands of these customers could lead to a cancellation or reduction of business from these customers. In addition, loss, cancellation or reduction of business from, significant changes in scheduled deliveries to, or decreases in the prices of products sold to any of these customers could significantly reduce our revenues and adversely affect our financial condition and operating results. Moreover, any difficulty in collecting outstanding amounts due from our customers particularly customers who place large orders, would harm our financial performance. In addition, if our relationships with our largest customers are disrupted for any reason, it could have a significant impact on our business.

***If the semiconductor industry suffers a shortage of flash memory, which is a key component in many of our and our customers' end products, our revenues could be adversely affected. Additionally, shortage of flash memory could cause the price of flash memory to increase, which could cause the price of client SSDs to increase and could negatively affect demand for SSDs and our controllers.***

During many periods in past years, some of our customers have indicated that they were unable to acquire enough NAND flash memory to meet all of the anticipated demand for their products. Several manufacturers of flash memory have increased or are planning to increase manufacturing capacity for flash memory. However, we cannot assure you that there will continue to be enough additional capacity to satisfy worldwide demand for flash memory. Because flash memory is a key component in solid state storage devices, if any shortage in the supply of flash memory occurs and is not remedied, our flash memory customers may limit their allocation of flash memory to client SSDs and our module maker customers may not be able to purchase enough flash memory to manufacture storage devices products and both types of customers may therefore purchase fewer controllers from us than they would have otherwise purchased. We also manufacture specialty SSD solutions using our controller technology and flash memory supplied to us by our customers or independently procured by us and our sales of SSD solutions will be adversely affected if we receive inadequate supplies of flash memory. Our ability to increase revenues and grow our profits could be materially and adversely affected as a result of any shortage or decrease in the supply of flash memory.

When the flash memory industry experiences a supply shortage, the price of flash memory could increase. As flash memory is the primary component in SSDs, when the price of flash memory increases, the price of SSDs could correspondingly also increase. Increases in client SSD prices could reduce demand for client SSDs because demand for client SSDs are among the most price sensitive of all major applications that use flash memory as many client applications can also switch to using low cost HDDs. Any decrease in demand for client SSDs could also reduce demand for our client SSD controllers.

***We operate in a rapidly changing industry where a significant majority of our sales are controllers used in solid state storage devices, and our failure to anticipate and respond quickly to changing industry trends relating to technology, standards, and consumer demand could adversely affect our growth and profitability.***

We operate in an intensely competitive industry that experiences rapid technological developments, changes in industry standards, changes in customer requirements, and frequent new product introductions and improvements. If we are unable to respond quickly and successfully to these developments, we may lose our competitive position, and our products or technologies may become uncompetitive. To compete successfully, we



must maintain a successful R&D effort to develop new product technologies at the same pace or ahead of our competitors. Many types of events could have a variety of negative effects on our overall competitive position and our financial results, such as reducing our revenue, increasing our costs, lowering our gross margin percentage, lowering our operating profitability and requiring us to recognize impairments on our assets. We may not be able to develop and market new products successfully, new markets at which our products target may not grow as expected, the products we invest in and develop may not be well received by customers, and products developed and new technologies offered by others may affect demand for our products.

Currently, a significant majority of our sales are controllers used in solid state storage devices. If new technologies for storing digital media are developed that compete with flash memory technology or render it obsolete and if we are not able to shift our product offerings accordingly, demand for our products would likely decline and our business would be materially and adversely affected.

In addition, we may not have sufficient management resources to manage, R&D capabilities to address, and financial resources to fund all of the required research to develop future innovations and meet changing industry standards. Moreover, even if we have adequate management resources, R&D capabilities, and financial resources, our future innovations may be outpaced by competing innovations. As a result, we may lose customers and significant sales, and our business and operating results may be materially and adversely affected.

***We may be unsuccessful in developing and selling new products or in penetrating new markets required to maintain our competitiveness or expand our business.***

We expect that a high percentage of our future sales will come from sales of new products. We sell products in markets that are characterized by rapid technological change, evolving industry standards, frequent new product introductions and products with short life cycles. The markets for some of these products are extremely competitive and may entail technologies that are new, immature and/or unpredictable to us. These markets and our endeavors to meet the markets may not develop into profitable opportunities and we have in the past invested substantial resources in emerging technologies that did not achieve the market acceptance and generate returns that we had expected. Recently, we have made significant investments in embedded storage controller technologies, especially those relating to SSDs. Failure to grow our embedded storage products or to recoup on our investments in these and other technologies could materially and adversely affect our results of operations and future business outlook. As a result, it is difficult to anticipate our future revenue streams from, or provide assurances on the success and the sustainability of, our new products.

***The average selling prices of our controller ICs have historically decreased and will likely do so in the future, which could harm our revenue and profitability.***

The controller ICs we develop and sell, especially those for expandable and embedded storage solutions, are used for high volume applications and have historically decreased over time, and we believe that it is possible they may also fall in the future. We may experience period-to-period fluctuations in future operating results if our average selling prices decline. We may be forced to reduce the average unit price of our products in response to new product introductions by our competitors, competitive pricing pressures and other factors. The mobile and computing devices markets are extremely cost sensitive, which may result in rapidly declining average selling prices of electronic devices and components, such as those made by us, used in devices and create downward pressure on our average selling prices and operating results. To maintain acceptable operating results, we will need to develop and introduce new products and product enhancements on a timely basis and continue to reduce our costs. We have also introduced products for the embedded storage market that typically experiences less intense competition. If we are unable to offset any reductions in our average selling prices by increasing our sales volumes or reducing corresponding production costs, or if we fail to gain more successes with embedded products or if we fail to develop and introduce new products and enhancements on a timely basis, our sales and operating results will be materially and adversely affected.

***If we are unable to accurately predict our future sales and to appropriately budget for our expenses, our results of operations could suffer.***

The rapidly changing nature of the global economy and the markets in which we sell our products limits our ability to accurately forecast quarterly and annual sales. Because many of our expenses are fixed in the short term or are incurred in advance of anticipated sales, we may not be able to decrease our expenses in a timely manner to offset any shortfall of sales, or expand our R&D and other operating infrastructure in a timely manner to capture anticipated business opportunities. If we expand our business operations and demand for our products does not increase as we may have projected, our operating results could be affected by our higher operating expense levels. Conversely, if we maintain or reduce our business operations and related expenses in accordance with our projections and demand for our products increases more than expected, our operating results could be affected by lost business opportunity, less competitive economies of scale, and damaged relationships with our customers.

***A failure to accurately forecast customer demand may result in excess or insufficient inventory, which may increase our operating costs and harm our business.***

To ensure the availability of our products for our customers, in some cases we cause our manufacturers to begin manufacturing our products based on forecasts provided by these customers in advance of receiving purchase orders. However, these forecasts do not represent binding purchase commitments, and we do not recognize revenue from these products until they are shipped to the customer. As a result, we incur inventory and manufacturing costs in advance of anticipated revenue. Because demand for our products may not materialize, manufacturing based on forecasts subjects us to risks of high inventory carrying costs and increased obsolescence and may increase our costs. If we overestimate customer demand for our products or if purchase orders are cancelled or shipments delayed, we may end up with excess inventory that we cannot sell, which could have a material and adverse effect on our financial results. Conversely, if we underestimate demand, we may not have sufficient product inventory and may lose market share and damage customer relationships, which could also harm our business.

***The loss of any of our key personnel or the failure to attract or retain specialized technical and management personnel could impair our ability to grow our business.***

We rely heavily on the services of our key employees, including Wallace C. Kou, our President and Chief Executive Officer. In addition, our engineers and other key technical personnel are a significant asset and are the source of our technological and product innovations. We believe our future success will depend upon our ability to retain these key employees and our ability to attract and retain other skilled managerial, engineering, technical and sales and marketing personnel. The competition for such personnel, particularly technical personnel, is intense in our industry. We may not be successful in attracting and retaining sufficient numbers of technical personnel to support our anticipated growth. These technical personnel are required to design and develop integrated circuits, including firmware, and to introduce product enhancements for use in future applications. Despite the incentives we provide, our current employees may not continue to work for us, and if additional personnel were required for our operations, we may not be able to obtain the services of additional personnel necessary for our growth. In addition, we do not maintain “key person” life insurance for any of our senior managers or other key employees. The loss of any of our key employees or our inability to attract or retain qualified personnel, including engineers, could delay the development and introduction of, and have an adverse effect on our ability to sell, our products as well as have an adverse effect on our overall growth. In addition, if any other members of our senior management or any of our other key personnel join a competitor or form a competing company, we may not be able to replace them easily and we may lose customers, business partners, key professionals and staff members. Substantially all of our senior executives and key personnel have entered into confidentiality and non-disclosure agreements. In the event of a dispute between any of our senior executives or key personnel and our operating companies in Taiwan, China or Korea, we cannot assure you the extent, if any, to which these provisions may be enforceable in Taiwan, China, or Korea due to the constantly evolving nature of the Taiwanese, Chinese, and Korean legal systems.

***We may not be able to deliver our products on a timely basis if our relationships with our suppliers, our semiconductor foundries or our assembly and test subcontractors are disrupted or terminated.***

We do not own or operate semiconductor fabrication facilities. Instead, we rely on third parties to manufacture our semiconductors. Two outside foundries, Taiwan Semiconductor Manufacturing Company (“TSMC”) and Semiconductor Manufacturing International Corporation (“SMIC”), with fabs in Taiwan, Singapore, and China currently manufacture the majority of our semiconductors. As a result, we face several significant risks, including higher wafer prices, availability of wafers and other raw materials, lack of manufacturing capacity, quality assurance, manufacturing yields and production costs, limited control over delivery schedules and product quality, increased exposure to potential misappropriation of our intellectual property, labor shortages or strikes and actions taken by third party contractors that breach our agreements.

The ability of each foundry to provide us with semiconductors is limited by its available capacity and access to wafers. We do not have long-term agreements with any of these foundries and we place orders on a purchase order basis. We place our orders based on our customers’ purchase orders and sales forecasts. However, the foundries can allocate capacity to the production of the products of their other customers and reduce deliveries to us on short notice or increase the price they charge us. It is possible that other foundry customers that are larger and better financed than we are, or have long-term agreements with these foundries, may induce these foundries to reallocate capacity to them. Any reallocation could impair our ability to secure manufacturing capacity that we need for our products. In addition, interruptions to the wafer manufacturing processes caused by a natural disaster or human error could result in partial or complete disruption in supply until manufacturing is re-started or we are able to shift manufacturing to another fabrication facility. It may not be possible to obtain sufficient capacity or comparable production costs at another foundry. Migrating our design methodology to a new third-party foundry could involve increased costs, resources and development time comparable to a new product development effort. Any reduction in the supply of semiconductors for our products could significantly delay our ability to ship our products and potentially have negative effects on our relationships with existing customers and our results of operations. In addition, if our subcontractors terminate their relationships with us, we would be required to qualify new subcontractors, which could take at least six months, resulting in unforeseen operating problems, and our operating results may be materially and adversely affected.

***If the foundries that provide us with the products for our operations do not achieve satisfactory yield or quality, or if the assembly and testing services fail us in the quality of their output, then our revenue, operating results and customer relationships will be affected.***

The manufacture of semiconductors is a highly complex process. Minor deviations in the manufacturing process can cause substantial decreases in yield. In some situations, such deviations may cause production to be suspended. The foundries that manufacture our semiconductors have from time to time experienced lower than anticipated manufacturing yields, including yields for our semiconductors, typically during the production of new products or architectures or during the installation and start-up and ramp-up of new process technologies or equipment. If the foundries that manufacture our semiconductors do not achieve planned yields, our product costs could increase and product availability would decrease.

After the wafer fabrication processes, our wafers are shipped to our assembly and testing subcontractors. We have a system to maximize consistent product quality, reliability and yield that involves our quality assurance team working closely with subcontractors in the various phases of the assembly and testing processes. Our supplier quality management includes procedures such as processes to pre-qualify our manufacturing suppliers and subcontractors. However, despite our efforts to strengthen supplier quality management, if our foundries fail to deliver fabricated silicon wafers of satisfactory quality in the volume and at the price we require, or if our assembly and testing subcontractors fail to efficiently and accurately assemble and test our products, we will be unable to meet our customers’ demand for our products or to sell those products at an acceptable profit margin, which would have a material and adverse effect on our sales and margins and damage our customer relationships.

***Failure to protect our proprietary technologies or maintain the right to certain technologies may negatively affect our ability to compete.***

We believe that the protection of our intellectual property rights is and will continue to be important to the success of our business. We rely on a combination of patent, copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. We also enter into confidentiality or license agreements with our employees, business partners and other third parties, and have implemented procedures to control access to and distribution of our documentation and other proprietary information. Despite these efforts, we cannot assure you that these measures will provide meaningful protection of our intellectual property rights. Further, these agreements do not prevent others from independently developing technologies that are equivalent to or superior to our technology. In addition, unauthorized parties may attempt to copy or otherwise obtain and use our proprietary technology. Monitoring unauthorized use of our technology is difficult and we cannot be certain that the steps we have taken will prevent unauthorized use of our technology, particularly in foreign countries such as Taiwan, Korea, and China where the laws may not protect our proprietary rights as fully as do the laws of the United States. In addition, if the foundries that manufacture our semiconductors lose control of our intellectual property, it could be more difficult for us to take remedial measures because our foundries are located in countries that do not have the same protection for intellectual property that is provided in the United States. Also, some of our contracts, including license agreements, are subject to termination upon certain types of change-of-control transactions.

As of March 31, 2018, we have 1,202 patents and 888 pending applications worldwide. We cannot be certain that patents will be issued as a result of our pending applications nor can we be certain that any issued patents would protect or benefit us or give us adequate protection from competing products. For example, issued patents may be circumvented or challenged and declared invalid or unenforceable or provide only limited protection for our technologies. We also cannot be certain that others will not design around our patented technology, independently develop our unpatented proprietary technology or develop effective competing technologies on their own.

***Failure to successfully defend against intellectual property lawsuits brought against us may adversely affect our business.***

Companies in and related to the semiconductor industry often aggressively protect and pursue their intellectual property rights. From time to time, we have received, and may continue to receive, notices that claim we have infringed upon, misappropriated or misused other parties' proprietary rights. Moreover, in the past we were in litigation with parties that claim that we infringed their patents or misappropriated or misused their trade secrets. In addition, we or our customers may be sued by other parties that claim that our products have infringed their patents or misappropriated or misused their trade secrets, or that may seek to invalidate one or more of our patents. An adverse determination in any of these types of disputes could prevent us from manufacturing or selling some of our products, increase our costs of revenue and expose us to significant liability. Any of these claims may materially and adversely affect our business, financial condition and results of operations. For example, in a patent or trade secret action, a court could issue a preliminary or permanent injunction that would require us or our customer(s) to withdraw or recall certain products from the market or redesign certain products offered for sales or under development. We may also be liable for damages for past infringement and royalties for future use of certain technologies. See "Legal Proceedings" below.

In addition, any litigation to defend ourselves against claims that we have infringed the intellectual property rights of others, could, regardless of the ultimate outcome, materially and adversely affect our operating results by requiring us to incur significant legal expenses and diverting the resources of the company and the attention of our management team.



***Because the markets in which we compete are highly competitive and many of our competitors have greater resources than we have, we cannot be certain that our products will compete favorably in the marketplace.***

We face competition from a number of competitors, including Marvell and our flash memory customers. We expect to face competition in the future from our current and potential competitors. In addition, some of our flash memory customers have developed products and technologies that could replace their need for our products or otherwise reduce their demand for our products.

Some of our current and potential competitors have longer operating histories, greater name recognition, access to larger customer bases and significantly greater financial, sales and marketing, manufacturing, distribution, technical and other resources than we have. As a result, they may be able to respond more quickly to changing customer demands or to devote greater resources to the development, promotion and sales of their products than we can. Our current and potential competitors may develop and introduce new products that will be priced lower, provide superior performance or achieve greater market acceptance than our products. For our SSD solutions, if we are unable to procure sufficient supplies of flash memory, our customers may seek to purchase SSD solutions from other suppliers.

***Our products must meet exacting specifications and undetected defects and failures may occur, which may cause customers to return or stop buying our products and may expose us to product liability risk and risks of indemnification against defects in our products.***

Our products are complex and may contain undetected hardware or software defects or failures, especially when first introduced or when new versions are released. These errors could cause us to incur significant re-engineering costs, divert the attention of our engineering personnel from product development efforts and materially affect our customer relations and business reputation. If we deliver products with errors or defects, our credibility and the market acceptance and sales of our products could be harmed. Defects could also lead to liability for defective products as a result of lawsuits against us or against our customers. We have agreed to indemnify some of our customers in some circumstances against liability from defects in our products. A successful warranty or product liability claim could require us to make significant payments.

***Our intellectual property indemnification practices may adversely impact our business.***

We may be required to indemnify our customers and our third-party intellectual property providers for certain costs and damages of intellectual property infringement in circumstances where our products are a factor in creating infringement exposure. In the contracts under which we sell semiconductor products, we may have agreed to indemnify our customers against losses arising out of claims of unauthorized use of intellectual property. In some of our licensing agreements, we have agreed to indemnify the licensee against losses arising out of or related to our conduct or services. We cannot assure you that claims for indemnification will not be made or that these claims would not have a material and adverse effect on our business, operating results or financial condition.

***We are exposed to potential impairment charges on intangible assets relating to recent acquisitions and on investments if business conditions deteriorate.***

We are required to perform testing for impairment losses relating to long-lived assets used in operations when indicators of impairment, such as reductions in demand or significant economic slowdowns in our business, are present. Through our acquisitions of FCI and other assets, we acquired core technology, customer relationships, goodwill and other intangible assets. The carry value of goodwill relating to these acquisitions must be assessed for impairment at least on an annual basis. In November 2009, we recorded US\$6.6 million of impairment charges relating to our long-lived assets and determined that our goodwill balance was impaired, and wrote down the goodwill balance by US\$30.8 million. In July 2015, we recorded US\$33.2 million of goodwill and US\$8.4 million of developed technology and in-process research and development from the acquisition of Shannon Systems. In July 2017, we recorded US\$0.6 million of goodwill and US\$4.7 million of know-how and

current technology from the acquisition of Bigtera. We performed our annual impairment assessment of the carrying value of FCI in November 2017 and determined that the goodwill balance was impaired, and wrote down the goodwill balance by US\$10.3 million. As of December 31, 2017, we had goodwill associated with our acquisitions of US\$59.0 million and intangible assets of US\$7.4 million. Although we recorded an impairment charges on goodwill and other long-lived assets in 2009 and 2017, we cannot be certain that these assets will not be subject to further write-downs in future periods and may record further impairment charges if sales of our specialty RF ICs, enterprise SSDs and software-defined storage do not grow as expected.

Separately, we also make minority stake investments in companies. If the companies in which we have invested are unable to execute their plans and succeed in their respective markets, we may not benefit from such investments, and we could potentially lose the amounts we invested. We evaluate our investments on a regular basis to determine if impairments have occurred and have recorded impairment charges in past years. These and future impairment charges could have a material and adverse impact on our operating results. We recognized impairment charges of US\$13 thousand on our investments in Cashido in 2016 and US\$120 thousand in Cashido and Vastview in 2017.

***Any failure to achieve and maintain effective internal controls could have a material adverse effect on our business, results of operations and the market price of our ADSs.***

We are subject to reporting obligations under securities laws of the United States. The Securities and Exchange Commission, or the SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, adopted rules requiring every public company to include in its annual report management's assessment of the effectiveness of the company's internal controls over financial reporting. In addition, an independent registered public accounting firm must attest to and report on the effectiveness of the company's internal controls over financial reporting.

Our management and independent registered public accounting firm have concluded that our internal controls as of December 31, 2017 are effective. However, we cannot assure you that in the future we or our independent registered public accounting firm will not identify material weakness during the audit process or for other reasons. In addition, 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. As a result, if we fail to maintain effective internal controls over financial reporting or should we be unable to prevent or detect material misstatements due to error or fraud on a timely basis, investors could lose confidence in the reliability of our financial statements, which in turn could harm our business and results of operations, negatively impact the market price of our ADSs and harm our reputation.

***We are subject to cybersecurity risk.***

We experience cyberattacks of varying degrees on our technology infrastructure and systems and, as a result, unauthorized parties have obtained in the past, and may in the future obtain, access to our computer systems and networks. The technology infrastructure and systems of our suppliers, vendors and partners may also experience such attacks. Cyberattacks are external and internal threats that include, but are not limited to, malware, phishing, advanced persistent threats, denial of service attacks, malicious software downloads, insider security breaches, and hardware and software vulnerabilities. We believe cyberattack attempts are increasing in number and that cyberattackers are developing increasingly sophisticated systems and means to not only attack systems, but also to evade detection or to obscure their activities.

We have controls and policies in place, will continue to enhance our capabilities and upgrade our protective solutions to guard against known and emerging threats, detect malicious or unauthorized activities, and have recovery systems to minimize business disruptions. If efforts to breach our infrastructure and systems are successful or we are unable to protect against these risks, we could suffer interruptions, delays, or cessation of

operations of our systems, and loss or misuse of proprietary or confidential information, IP, or sensitive or personal information. Breaches of our infrastructure and systems could also cause our customers and other affected third parties to suffer loss or misuse of proprietary or confidential information, IP, or sensitive or personal information, and could harm our relationships with customers and other third parties. As a result, we could experience additional costs, indemnification claims, litigation, and damage to our brand and reputation. All of these consequences could harm our reputation and our business and materially and adversely affect our operating results and financial condition.

***Laws and regulations to which we are subject, as well as customer requirements in the area of environmental protection and social responsibility, could impose substantial costs on us and may adversely affect our business.***

We are subject to various state, federal and international laws and regulations governing the environment, including restricting the presence of certain substances in electronic products. In addition, we are also subject to various industry requirements restricting the presence of certain substances in electronic products. Although our management systems are designed to maintain compliance, we cannot assure you that we have been or will be at all times in complete compliance with such laws and regulations. If we violate or fail to comply with any of them, a range of consequences could result, including fines, import/export restrictions, sales limitations, criminal and civil liabilities or other sanctions.

Recently there has been increased focus on environmental protection and social responsibility initiatives, which are subject to change, can be unpredictable, and may be difficult for us to comply with, given the complexity of our supply chain and our significant outsourced manufacturing. We are required to implement various standards or processes due to the adoption of rules or regulations that result from these initiatives, such as the SEC rules on the disclosure of the use of “conflict minerals.” If we are unable to comply, or ensure that our suppliers or contract manufacturers comply, with such standards or processes, customers may stop purchasing from us, which could adversely affect our sales and results of operations.

***Our stock price has been, and may continue to be, volatile, which could result in investors losing all or part of their investments.***

Since we completed our initial public offering in June 2005, the market price of our ADSs has been and likely will continue to be highly volatile and could be subject to wide fluctuations in response to numerous factors, including the following:

- actual or anticipated variations in our quarterly operating results or those of our competitors, customers, or NAND flash vendors;
- actual or anticipated changes in NAND flash supply-demand dynamics;
- actual or anticipated changes in our market share or the market share of our competitors;
- the commencement or results of litigation;
- announcements by us, our competitors, our customers, or their other suppliers of new products or technological innovations;
- changes in financial estimates or recommendations by securities analysts;
- the payment or non-payment of cash dividends at the discretion of our board of directors;
- the announcement and implementation of share repurchase programs;
- announcements by us or our competitors of significant acquisitions, divestitures or partnerships; and
- actual or anticipated changes in the global economic or industry outlook.

Many of these factors are beyond our control and may negatively impact the market price of our ADSs, regardless of our performance. In addition, the stock market in general, and the market for technology and semiconductor companies in particular, have been highly volatile. Our ADSs may not trade at the same price levels as that of other semiconductor and technology companies, and shares of semiconductor and technology companies, in general, may not sustain their current market prices. These fluctuations as well as general economic, political, and market conditions may have an adverse effect on the market price of our ADSs.

***There can be no assurance that we will continue to declare cash dividends on a quarterly basis, if at all or in any particular amounts.***

Our Board of Directors declared payment of our first quarterly dividend on our common stock in January 2013 and the first dividend payment was made on March 4, 2013. Our Board of Directors has subsequently declared and paid dividends in each successive quarter. On October 24, 2016 and 2017, our Board of Directors, instead of declaring a quarterly dividend, declared an annual dividend payable in four quarterly installments. The continuation of declaring dividends or if at all, depends on, among other things, that the dividend payment is in the best interests of our shareholders, our results of operations, capital availability and future capital requirements, financial condition, statutory requirements, and other factors that the board of directors may deem relevant. The decision of any declaration of dividend payment, the amount and the frequency of such, if at all, is the discretion of our Board of Directors. Our dividend payments may change from time to time, and we cannot provide assurance that we will continue to declare dividends, if at all or in any particular amounts. A reduction in or elimination of our dividend payments could have a negative effect on our share price.

***If we are characterized as a passive foreign investment company, U.S. Holders may experience adverse tax consequences.***

Based on the present and projected composition of our income and valuation of our assets, we believe we are not currently classified as a passive foreign investment company (“PFIC”) for U.S. federal income tax purposes. We will generally be classified as a PFIC for any taxable year in which either (a) at least 75% of our gross income is passive income or (b) at least 50% of the value (determined on the basis of a quarterly average) of our assets is attributable to assets that produce or are held for the production of passive income. If we are characterized as a PFIC, U.S. Holders may experience adverse tax consequences. See “ITEM 10. ADDITIONAL INFORMATION — Taxation — United States Federal Income Taxation.”

***We are subject to risks associated with international operations which may harm our business.***

We conduct our business worldwide. We are a Cayman Islands corporation with principal executive offices in Hong Kong and have most of our operations outside of the United States. We undertake our design and development activities primarily in China, Korea and Taiwan. Our integrated circuits are manufactured, assembled, tested and packaged by third-parties located primarily in China, Korea, and Taiwan. We generated 89%, 89% and 92% of our revenue in 2015, 2016 and 2017, respectively, from sales to customers outside the United States, and for the year ended December 31, 2017, 72% of our revenue was from sales in three jurisdictions — Taiwan, Korea and China. International operations are subject to many other inherent risks, including but not limited to:

- international economic and political conditions, such as political tensions between countries in which we do business (please also refer to Risk Factors relating to China, Korea, and Taiwan);
- unexpected changes in, or impositions of, legislative or regulatory requirements;
- complying with a variety of foreign laws;
- differing legal standards with respect to protection of intellectual property and employment practices;
- cultural differences in the conduct of business;

- inadequate local infrastructure that could result in business disruptions;
- exporting or importing issues related to export or import restrictions, tariffs, quotas and other trade barriers and restrictions;
- financial risks such as longer payment cycles and difficulty in collecting accounts receivable;
- adverse taxes rules, regulations and penalties; and
- other factors beyond our control such as nature disasters, terrorism, civil unrest, war and diseases such as severe acute respiratory syndrome, the Avian influenza, and the Swine influenza.

Although our reporting currency is the U.S. dollar, and the majority of our sales and cost of sales are denominated in the U.S. dollar, the majority of our operating expenses are denominated in the NT dollar, and to a lesser extent Korean won, Chinese yuan and U.S. dollar. The functional currencies of our Korean operations and our Chinese operations are the Korean Won and the Chinese yuan, respectively. As a result, appreciation or depreciation of other currencies in relation to the U.S. dollar could result in material transaction and 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.

***We operate primarily in regions that are susceptible to natural disasters.***

Parts of the world, including Taiwan, Japan, China and the United States are susceptible to earthquakes. In 1999, 2008, and 2011, Taiwan, China, and Japan respectively, experienced severe earthquakes that caused significant property damage and loss of life. Although the 1999, 2008 and 2011 earthquakes did not have a material impact on our business, and the region has not suffered such a major earthquake in many years, the occurrence of such an event is unpredictable, and a major earthquake and consequent disruptive events could severely disrupt the normal operations of our business and have a material and adverse effect on our financial condition and operating results.

***We face substantial political risks associated with doing business in Taiwan because of the tense political relationship between Taiwan and the People's Republic of China.***

A majority of our employees and a significant portion of our research and development and operations are based in Taiwan. In addition, most of our foundries and assembly and testing suppliers such as TSMC, SMIC, Advanced Semiconductor Engineering Group (“ASE”), Siliconware Precision Industries Co., Ltd. (“SPIL”), and King Yuan Electronics Corp. (“KYECC”) are located in either Taiwan or China. Accordingly, our business and results of operations and the market price of our ADSs may be affected by changes in Taiwan or China governmental policies, taxation, inflation or interest rates and by social instability and diplomatic and social developments in or affecting Taiwan that are outside of our control. Taiwan has a unique international political status. China does not recognize the sovereignty of Taiwan. Although there have been significant economic and cultural ties between Taiwan and China in recent years, the political relations have often been strained. The government of China has indicated that it may use military force to gain control over Taiwan, particularly under what it considers as highly provocative circumstances, such as a declaration of independence by Taiwan or the refusal by Taiwan to accept China’s “One China” policy. On March 14, 2005, the National People’s Congress of China passed what is widely referred to as the “anti-secession” law, a law authorizing the Chinese military to attack Taiwan in order to block moves by Taiwan toward formalizing independence.

Past and recent developments in relations between Taiwan and China have on occasion depressed the market prices of the securities of Taiwanese companies or companies with significant business activities in Taiwan. We cannot assure you any contentious situations between Taiwan and China will always resolve in maintaining the current status quo or remain peaceful. Relations between Taiwan and China and other factors affecting military, political or economic conditions in Taiwan could have a material adverse effect on our financial condition and results of operations, as well as the market price and the liquidity of our ADSs.



***We face substantial political risk associated from doing business in South Korea because of tensions in the political relationship between South Korea and North Korea.***

Relations between South Korea and North Korea have been tense over most of South Korea's history. In recent years, there have been heightened security concerns stemming from North Korea's nuclear weapons and ballistic missile capabilities and uncertainty regarding North Korea's actions and possible responses from the international community. More recent concerns over North Korea's nuclear and ballistic missile testing programs, hostile and threatened actions by North Korea against South Korea, North Korea's leadership succession, and relations between the United States and North Korea, have created a global security issue that may adversely affect South Korean business and economic conditions. South Korea was not a signatory of the armistice agreement that ended the Korean War, and since no peace treaty was signed between South Korea and North Korea, the two countries are technically still at war. We cannot assure you as to whether or when this situation will be resolved or change abruptly as a result of current or future events, including, without limitation, the effects, if any, of (i) the transition of the "Supreme Leader" to Kim Jong Un that began after the passing of Kim Jong Il in 2011, (ii) recent increases to previously imposed UN sanctions on North Korea, (iii) the effects of the denial of access to South Koreans who manage jointly run factories in the North Korean city of Kaesong and (iv) the general increase in overtures and rhetoric by the North Korean government with respect to its nuclear capabilities and willingness to use such weapons as they see fit. Although talks have recently been held between South Korea and North Korea and are preliminarily scheduled between the U.S. and North Korea, political instability has generally increased with the current U.S. administration. We cannot give any assurance that the level of instability and tension in the Korean peninsula will not escalate in the future, or that the political regime in North Korea may not suddenly collapse. An adverse change in economic or political conditions in South Korea or North Korea or in South Korea's relations with North Korea could have a material adverse effect on our South Korean subsidiary and our company.

***Our business depends on the support of the Taiwanese and South Korean governments, and a decrease in this support may increase our tax liabilities and decrease our net income.***

Our Taiwan operating company has benefited from tax incentives provided by the Taiwanese government. For example, under the Statute for Upgrading Industries of Taiwan, we were granted tax credits by the Taiwan Ministry of Finance for qualifying research and development costs and in qualifying employee training expenses. In addition, Taiwan law offers preferential tax treatments to industries that are encouraged by the government. In 2010, "Statute for Industries Innovation" was passed to replace the "Statute for Upgrading Industries" in tax incentives. However, we are still eligible to use certain previously granted exemptions. See "Operating and Financial Review and Prospects — Principal Factors Affecting Our Results of Operations — Provision for income taxes" and Note 15 to our consolidated financial statements for a more detailed description of our ability to enjoy these preferential tax treatments. If any of our tax credits or our ability to take advantage of these preferential tax treatments are curtailed or eliminated, our net income may decrease materially. The last tax credit granted to us by the Taiwanese government expired at the end of 2016.

The South Korean government provides a variety of tax incentives designed to promote designated industries such as the technology industry. We, like many Korean technology companies, have benefited from certain tax incentives, including tax credits for applicable research and development expenses and for investments made to improve business productivity. If these and other tax incentives are curtailed or eliminated, our net income may decrease materially.

***The enactment of legislation implementing changes in taxation of international business activities, the adoption of other tax reform policies or changes in tax legislation or policies could materially impact our financial position and results of operations.***

Tax bills are introduced from time to time to reform taxation of international business activities. The Organisation for Economic Co-operation and Development, or OECD, has released guidance covering various topics, including country-by-country reporting, definitional changes to permanent establishment and guidelines

in determining arm’s length transfer pricing. This guidance is collectively referred to as Base Erosion and Profit Shifting, or BEPS, an initiative that aims to standardize and modernize global tax policy. Depending on legislation ultimately enacted in connection with this guidance by jurisdictions in which we operate, there may be significant consequences for us due to our significant international business activities. For example, adoption of BEPS by foreign jurisdictions in which we operate could result in changes to tax policies, including transfer-pricing policies that could ultimately impact our tax liabilities to foreign jurisdictions. If any of these proposals are enacted into law, or if other international, consensus-based tax policies and principles are amended or implemented, they could have material adverse consequences on the amount of tax we pay and thereby on our financial position and results of operations.

In addition, policies regarding corporate income taxes in numerous jurisdictions are under heightened scrutiny. As a result, decisions by tax authorities regarding treatments and positions of corporate income taxes could be subject to legislative investigation and inquiry, which could result in changes in tax policies or prior tax rulings. As such, the taxes we previously paid may be subject to change and our taxes may increase in the future, which could have an adverse effect on our results of operations, financial condition and our corporate reputation.

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

##### **History and Development of the Company**

Silicon Motion Technology Corporation (“Silicon Motion”) is a corporation which was incorporated in the Cayman Islands in January 2005 and acquired Silicon Motion, Inc., a Taiwan corporation (“SMI Taiwan”), in April 2005. Originally SMI Taiwan was known as Feiya Technology Corporation (“Feiya”), a Taiwan corporation which was incorporated in April 1997 but had changed its name to SMI Taiwan after acquiring in August 2002 Silicon Motion, Inc., a California corporation (“SMI USA”), which was incorporated in November 1995. Feiya was originally a flash memory products company and SMI USA a graphics processor company. In April 2007, we acquired FCI Inc. (“FCI”), a leading designer of RF ICs for mobile TV and wireless communications based in Korea. In July 2015, we acquired Shanghai Baocun Information Technology Co., Ltd (“Shannon Systems”), China’s leading enterprise-class PCIe SSD company based in Shanghai, China. In July 2017, we acquired Bigtera, a software-defined storage company.

Our principal executive offices are located at Unit 04-05, 27/F, #909 Cheung Sha Wan Rd., Cheung Sha Wan, Kowloon, Hong Kong. The address of our United States operating subsidiary, Silicon Motion, Inc., is 690 N. McCarthy Blvd. Suite 200, Milpitas, CA 95035. The address of our Taiwan operating subsidiary, Silicon Motion, Inc., is 8/F, #36 Taiyuan St., Jhubei, Hsinchu 30265, Taiwan. Our ADSs, each representing four of our ordinary shares, have been listed and traded on Nasdaq since June 2005.

##### **Subsidiaries of the Company**

Below is a list of subsidiaries of the Company. All subsidiaries are wholly owned.

<u>Name of Entity</u>	<u>Jurisdiction of Incorporation</u>
FCI Inc.	Korea
Silicon Motion K.K.	Japan
Silicon Motion Korea Ltd.	Korea
Silicon Motion Technology (HK) Ltd.	Hong Kong
Silicon Motion, Inc.	California
Silicon Motion, Inc.	Taiwan
Silicon Motion, Inc. (Beijing)	China
Silicon Motion, Inc. (Shanghai)	China
Silicon Motion, Inc. (Shenzhen)	China
Shannon Systems	China
Bigtera Limited	Hong Kong

## Overview

We are a global leader and pioneer in developing NAND flash controller ICs for solid-state storage devices. We supply more NAND flash controllers than any other company in the world and have one of the broadest portfolios of controller solutions and technologies. Our key products are controllers used in embedded storage products such as SSDs, eMMCs, and UFS, as well as in expandable storage products such as memory cards and USB flash drives. Our products are widely used in computing and mobile devices and for industrial, enterprise, commercial and other applications. Our customers include most of the NAND flash makers, leading technology OEMs, and the majority of storage device module makers. More NAND flash products, especially next-generation flash, produced by Intel, Micron, Samsung, SK Hynix, Toshiba and Western Digital are supported by Silicon Motion controllers than any other company. We are the world's leading merchant supplier of controllers for eMMC embedded memory used in smartphones and tablets, and the leading merchant supplier of controllers for client SSDs used in PCs and other applications. We also supply customized specialty SSD solutions for the Chinese hyperscale data center market and for high-performance industrial applications. We market our controllers under the "SMI" brand, our enterprise-grade SSDs under the "Shannon" brand, our single-chip industrial-grade SSDs under the "Ferri SSD" and "Ferri-eMMC" brands, specialty RF ICs under the "FCI" brand, and software-defined storage under the "Bigtera" brand.

## Industry Background

We operate in the semiconductor industry and primarily focus on designing, developing and marketing: (i) controllers for managing NAND flash used in embedded storage applications, such as eMMC embedded memory and SSDs and expandable storage applications such as flash memory cards and USB flash drives, (ii) customized specialty SSD solutions for the Chinese hyperscale data center market and for high-performance industrial applications, and (iii) specialty RF ICs used in mobile devices.

### *Our Market and Products*

Our products, primarily embedded storage products, expandable storage products and specialty radio frequency integrated circuits (RF ICs), are designed, developed and marketed to mobile storage, enterprise storage, and mobile communications markets. The two general types of embedded storage and expandable storage products that we sell are (i) NAND flash controllers, such as embedded MultiMediaCard (eMMC), Universal Flash Storage (UFS), client solid-state drive (SSD), Secure Digital (SD) card and Universal Serial Bus (USB) flash drive controllers, and (ii) specialty storage solutions, such as our customized enterprise-grade Shannon Systems Peripheral Component Interconnect Express (PCIe) SSDs and industrial-grade and commercial-grade single-chip FerriSSDs and Ferri-eMMCs. NAND flash controllers account for a significant majority of sales. Our Ferri storage solutions all use our industry-proven controllers and beginning in 2016, Shannon SSDs also started using our controllers in selected products.

### *NAND Flash Controllers*

NAND flash is a type of non-volatile digital data storage technology that does not require power to retain data and has become the primary semiconductor technology for mass digital data storage. The benefits of NAND flash include high data storage capacity at low cost per bit, fast data read and write access time, low operating power requirements, small form-factor and shock resistance. NAND flash is widely used for embedded and expandable data storage in mobile and computing devices such as smartphones and notebook PCs and more recently is also being used in commercial-grade, industrial-grade, and enterprise-grade equipment. The NAND flash market is large and has grown rapidly, and the leading suppliers of NAND flash are Intel, Micron, Samsung, SK Hynix, Toshiba and Western Digital.

All NAND flash storage devices require a controller and almost all storage devices use a discrete controller IC. Key functions of a flash memory controller include:

- managing the interfacing of the NAND flash in the flash memory storage product with the host device;

- ensuring data reliability in NAND flash by detecting and correcting bit errors in the NAND flash caused by read/write disturbance and adjacent cell interference;
- ensuring data integrity in NAND flash by mapping bad blocks and preventing bad blocks from being used for storing data;
- maximizing the life of NAND flash with wear-leveling algorithms which spread out the use of the memory array and equalize the use of all the memory cells;
- enhancing the sequential and random read and write performance of NAND flash by utilizing multiple-plane architecture, interleaving, or other technologies;
- preventing data loss during sudden, unexpected host device power failures with advanced power cycling solutions;
- implementing security features to protect software code, personal data and multimedia digital rights; and
- ensuring that flash memory storage solutions are compatible with host devices.

We believe that our controllers are designed to meet the specifications of the majority of NAND flash components currently being produced by different flash memory manufacturers, including small and big block Single-Level Cell (“SLC”) and Multi-Level Cell (“MLC”) NAND flash. Most of our controllers support planar and 3D two-bits per cell MLC or three-bits per cell MLC NAND flash, which is also known as Triple-Level Cell (“TLC”) NAND flash. Our newly developed controllers also support 3D four-bit per cell MLC NAND, which is also known as Quad-Level Cell (“QLC”) NAND flash. Our controllers also support planar NAND flash designed and fabricated at all of the most advanced process geometries and 3D NAND flash designed and fabricated with the highest layer-count architecture.

### ***Mobile Storage Market***

We provide embedded storage products and expandable storage products primarily for the mobile storage market, targeting NAND flash makers, technology OEMs and module makers.

### **Embedded Storage Products**

*eMMC and UFS controllers.* We supply controllers for eMMC and UFS, both industry standard high-performance, low-power single-chip embedded memory solutions that are widely used in smartphones, tablets, smart TVs and other IOT devices. Our customers use our controllers with their NAND flash components to manufacture single-chip eMMC or UFS memory modules and with their NAND flash and mobile dynamic random-access memory (DRAM) components to manufacture eMMC-based multi-chip package (eMCP) and UFS-based multi-chip package (uMCP) memory modules. Our eMMC and UFS controllers support all the current widely used standards, including eMMC 4.5, eMMC 5.0, eMMC 5.1, UFS 2.0 and UFS 2.1. We believe we are the world’s largest merchant supplier of eMMC and UFS controllers. Our largest eMMC controller customer is SK Hynix; we believe SK Hynix is manufacturing eMMCs and eMCPs with our controllers and is supplying all of the global top 10 Android smartphone original equipment manufacturers (OEMs) with these solutions.

*Client SSD controllers.* We believe we are the world’s largest merchant supplier of client SSD controllers and provide highly customizable hardware plus firmware turnkey SSD controller solutions to NAND flash manufacturers and module makers that manufacture and supply to PC OEMs and the channel markets their SSDs with our controllers for use in notebook and desktop PCs, other client devices and in high-performance, low-latency non-mission critical data center applications. Our client SSD controllers support interfaces that include Serial Advanced Technology Attachment (SATA) III and PCIe Gen 3 and the majority of the latest generation of NAND flash components. Our value-added technologies provided to our client SSD controller customers include end-to-end data path protection, power-loss data security features, Opal-compliant AES advanced full-disk encryption, and active operating temperature monitoring.

*Embedded flash storage controllers.* Our embedded flash controllers are designed to control NAND flash embedded on devices with Compact Flash, USB, and SATA interfaces. Applications using our embedded flash storage controllers include industrial-grade and commercial-grade Compact Flash (CF) cards, Secure Digital (SD) cards, disk-on-modules (DOMs), Integrated Drive Electronics (IDE) SSDs (also known as Parallel Advanced Technology Attachment (PATA) SSDs), embedded and external USB flash drives and SATA SSDs. Our embedded flash controllers are offered in commercial temperature (0 °C to 70 °C) and industrial temperature (-40 °C to +85 °C) versions and backed by long term product support. We believe we are the world's largest supplier of embedded flash storage controllers and supply our controllers primarily to module makers that specialized in supplying the industrial and commercial applications markets.

*Ferri storage solutions.* Our *FerriSSDs* and *Ferri-eMMCs* are highly reliable, industrial-grade and commercial-grade single-chip SSDs, which are developed for a wide-range of embedded applications that require high data rate, small form factor and compliance with standard PATA, SATA, PCIe, eMMC and UFS protocols. These single-chip SSDs are designed using our industry-proven PATA, SATA, PCIe, eMMC, and UFS controller technologies with high-quality NAND flash components to simplify customers' design work, and are offered to OEM customers that also require long supply continuity. For certain customers, we offer options for firmware customization to meet their unique embedded storage requirements. We believe we are the world's largest supplier of industrial-grade and commercial-grade single-chip SSDs.

*Shannon enterprise SSD solutions.* In China, we provide customized, high-performance enterprise-grade SSDs for both hyperscale and enterprise data centers. Our SSDs are developed for customers who require the largest storage capacity, lowest latency, fastest input/output operations per second (IOPS), lowest power, feature-rich software functionality and unparalleled performance stability with end-to-end data path protection.

### **Expandable Storage Products**

*Flash memory card controllers.* Our controllers for flash memory card standards include microSD cards used primarily with smartphones and SD and CF cards used primarily with digital cameras and camcorders. For microSD and SD cards, we offer controllers for (i) different speed class, including the significantly faster Secure Digital High Capacity (SDHC) and Secure Digital eXtended Capacity (SDXC) cards that use the Ultra High Speed (UHS) bus and (ii) different storage capacities, including the significantly higher capacity SDHC and SDXC cards, which also have faster speed and added capabilities.

*USB flash drive controllers.* USB flash drives are NAND flash storage devices integrated with a standard USB interface, either USB 2.0 or the faster USB 3.0. USB flash drives are popular in computing and consumer electronics markets for the portable storage of files.

### **Mobile Communications Market**

For the mobile communications market, a market that extends from smartphones to new devices that target the internet-of-things, we provide specialty RF ICs, primarily mobile TV system-on-chips (SoCs) and low power WiFi SoCs.

*Mobile TV SoCs.* Our products include integrated mobile TV tuner plus demodulator SoCs for mobile phones and other portable devices. Our solutions are designed for leading digital mobile TV broadcast standards, specifically Terrestrial-Digital Media Broadcast (T-DMB) for the Korean market and Integrated Services Digital Broadcasting-Terrestrial (ISDB-T) for the Japanese and certain Asian and South American markets.

*Low Power Wi-Fi SoCs.* We offer ultra-low power Wi-Fi SoCs for addressing smart home, commercial, and industrial applications. Specific target applications include smart thermostats and other sensors, video surveillance cameras, smart door locks and video door bells.



## **Our Customers**

We sell our semiconductor solutions to NAND flash manufacturers, leading technology OEMs and module makers worldwide. Most of our high performance flash memory storage controllers are supplied to NAND flash manufacturers. We are a leading merchant supplier of controllers for SSDs used in PCs and other client devices, eMMC used in smartphones, flash memory cards and USB flash drives.

Sales to our five largest customers represented approximately 54%, 58% and 57% of our net revenue in 2015, 2016 and 2017, respectively. Sales to two customers in 2017, and one customer in 2015 and 2016 accounted for 10% or more of our net revenue, representing 30%, 28% and 39% of our net revenue in 2015, 2016 and 2017, respectively. In 2015 and 2016, the significant customer was SK Hynix and in 2017, SK Hynix and Intel. The identities of our largest customers and their respective contributions to our net revenue have varied and will likely continue to vary from period to period.

The majority of our customers purchase our products through purchase orders, as opposed to entering into long-term contracts with us. The price for our products is typically agreed upon at the time a purchase order is placed.

## **Sales and Marketing**

We market and sell our products worldwide through a combination of direct sales personnel and independent electronics distributors. Our direct sales personnel are strategically located near our NAND flash manufacturer, leading technology OEM and modular maker customers in Taiwan, Korea, China, the United States, and Japan. Approximately 71% of our sales in 2015, 69% of our sales in 2016, and 68% of our sales in 2017 were attributable to our direct sales force while the remainder was attributable to distributors.

To supplement our direct sales, we have independent electronics distributors and sales reps located throughout the world. We selected these distributors and reps based on their ability to provide effective field sales, marketing communications and technical support for our products to our customers.

Our marketing group focuses on our product strategy, product development road maps, new product introduction process, demand assessment, competitive analysis, and product marketing. We seek to work with potential and existing customers early in their design process to best match our products to their needs, and more broadly, to ensure that product development activities, product launches, and on-going demand and supply planning occur in a well-managed, timely basis in coordination with our research and development, operations, and sales groups, as well as our customers and distributors. We also attend industry tradeshows and technical conferences to promote our products and solutions, maintain close contact with our existing customers to assess demand, and keep current with industry trends. Our participation in industry standards associations, such as JEDEC and the SD Association for our embedded storage and expandable storage products, helps us monitor the latest industry developments and promote our corporate profile. Our marketing group also works with our sales teams to identify new business opportunities.

We also have field application engineers (FAEs), who provide technical support and assistance to existing and potential customers in designing, testing and qualifying systems that incorporate our products. Our FAE organization is segmented by product and market to support our customers.

## **Research and Development**

We devote a significant amount of resources to research and development for broadening and strengthening our portfolio of technology, products and solutions. Our engineering team has expertise in NAND flash management algorithms, system architecture, digital, mixed-signal and RF IC design, and software engineering. As of March 31, 2018, we have 1,202 patents and 888 pending applications worldwide. We will continue to actively pursue the filing of additional patent applications in important jurisdictions.

We believe technology research and product development is essential to our growth. Our primary research and development centers are located in Hsinchu and Taipei, Taiwan, Seoul, South Korea and Shanghai, China. Our facilities in Seoul focus primarily on our specialty RF IC products, our facilities in Hsinchu and Taipei focus primarily on our NAND flash controller products, and our facilities in Shanghai focus primarily on SSD solutions and specific product requirements of our customers in China.

Our research and development expenses were approximately US\$71.2 million, US\$92.4 million and US\$102.1 million for the years ended December 31, 2015, 2016 and 2017, respectively.

## **Manufacturing**

We design and develop our products and electronically transfer our proprietary designs to independent foundries for the manufacturing and processing of silicon wafers. Once the wafers are manufactured, they are then shipped to third-party assembly and testing subcontractors. Individual dies on each wafer are assembled into finished chips and undergo several stages of testing before delivery to our customers. We also ship bare dies to our customers. We believe that our strategy of outsourcing wafer fabrication, packaging and testing enables us to benefit from the research and development efforts of leading manufacturers without the requirement to commit our own substantial capital investments. Our fabless business model also provides us with the flexibility to engage vendors who offer services that best complement our products and technologies.

*Wafer fabrication.* TSMC and SMIC are currently our primary foundries that manufacture most of our semiconductors. We use their fabs in Taiwan, Singapore, and China to fabricate our devices using mature and stable CMOS process technology, primarily with process node from 28 to 55 nanometers. We regularly evaluate the benefits and feasibility, on a product-by-product basis, of migrating to more cost efficient manufacturing process technologies.

*Assembly and testing.* Following wafer fabrication, our wafers are shipped to our assembly and test subcontractors where they are probed, singulated into individual dies, assembled into packaged chips, and undergo the process of electronic final testing. In order to minimize cost and maximize turn-around time, our products are designed to use low cost, industry standard packages and can be tested with widely available automatic testing equipment. We currently engage companies such as ASE, SPIL, and KYEC as our primary subcontractors for the assembly and testing of our products. We have dedicated teams of manufacturing engineers who maintain control over the process from the early stages of manufacturing. Our engineers work closely with our subcontractors to develop product testing and packaging programs to ensure these programs meet our product specifications, thereby maintaining our ownership of the functional and parametric performance of our semiconductors.

*Quality and reliability assurance.* We have designed and implemented a quality assurance system that provides the framework for continual improvement of products, processes and customer service. To ensure consistent product quality, reliability and yield, our quality assurance teams perform reliability engineering, quality control, international organization for standardization (ISO) system development, document control, subcontractor quality management and customer engineering services to closely monitor the overall process from IC design to after-sale customer support. In particular, we rely on in-depth simulation studies, testing and practical application testing to validate and verify our products. We emphasize a strong supplier quality management practice in which our manufacturing suppliers and subcontractors are pre-qualified by our quality assurance teams. Our suppliers are required to have a quality management system, certified to ISO 9000 standard. Our operations have been ISO 9001 certified since 1999.

## **Competition**

We face competition from a number of competitors, including Marvell and our flash memory customers.

## Seasonality

See “Risk Factors — Because our operating results for any period could be adversely affected by a number of factors and therefore fluctuate significantly, our annual and quarterly operating results are difficult to predict” in Item 3 above and “Operating and Financial Review and Prospects — Principal Factors Affecting Our Results of Operations” in Item 5 below.

## Intellectual Property

Our success and future revenue growth depends, in part, on our ability to protect our intellectual property. We rely on a portfolio of intellectual property rights, registered in the United States, Taiwan, and other countries, including patents, copyrights, trademark registrations, trade secret laws, contractual provisions, licenses, and other methods to protect our intellectual property.

As of March 31, 2018, we have 1,202 patents and 888 pending applications worldwide. There can be no assurance that patents will ever be issued with respect to these pending applications. Furthermore, it is possible that any patents held by us may be invalidated, circumvented, challenged or licensed to others. In addition, there can be no assurance that such patents will provide us with competitive advantages or adequately safeguard our proprietary rights. While we continue to file new patent applications with respect to our recent developments, existing patents are granted for prescribed time periods and will expire at various times in the future. We expect to continue to file patent applications where appropriate to protect our proprietary technologies.

Companies in the semiconductor industry have frequently demonstrated a readiness to commence litigation based on allegations of patent and other intellectual property infringement. From time to time, third parties may assert infringement claims against us. We may not prevail in any such litigation or may not be able to license patents from third parties on commercially reasonable terms, if at all. Litigation, regardless of the outcome, is likely to result in substantial cost and diversion of our resources, including our management’s time. Any such litigation could materially adversely affect us. In addition, in the contracts under which we sell semiconductor products, we may have agreed to indemnify our customers against losses arising out of claims of unauthorized use of intellectual property.

We intend to protect our intellectual property rights vigorously, but there can be no assurance that our efforts will be successful. In addition, the laws of other countries in which our products are sold may not protect our products and intellectual property rights to the same extent as the laws of the United States.

While our ability to effectively compete depends in large part on our ability to protect our intellectual property, we believe that our technical expertise, customer support capabilities, and ability to introduce new products in a timely and cost effective manner will be important factors in maintaining our competitive position.

We claim copyright and trademark protection for proprietary documentation for our products and a variety of branding marks. We have registered “Silicon Motion” and its logo (a three-dimensional cube depiction of the letters “SM”), FCI, the FCI logo, the Shannon Systems logo, “PCIe-RAID,” “DIRECT-IO,” “Hyper-IO,” “airRF,” “basicRF,” “ezRF,” “ezSYS,” “powerRF,” “twinRF,” “zipRF,” “zipSYS,” “VirtualZero,” “SSDLifeGuard,” “SSDLifeSaver,” “TurboMLC,” “FerriSSD,” “Ferri-eMMC,” “Bigtera,” the Bigtera logo, the CAT logo, and “NANDXtend” as trademarks in the United States, Taiwan, and other countries.

We also attempt to protect our trade secrets and other proprietary information through agreements with our customers, suppliers, employees and consultants, and through other customary security measures.

We have entered into license agreements with third party intellectual property vendors for wafer fabrication tool libraries, semiconductor IP core, computer aided design tools, and software.

## Facilities

As of the date of this annual report, we occupy facilities totaling approximately 377,700 square feet, which house our management and administration, operations, research and development and sales and marketing departments. Of our facilities, approximately 202,600 square feet are owned and approximately 175,100 square feet are occupied under leases. We consider our facilities sufficient to meet our current operational requirements. The table below lists the location of our operating facilities.

<u>Location</u>	<u>Primary Use</u>	<u>Approximate Square Footage</u>
Jhubei, Taiwan . . . . .	Research & development, management & administration	182,600
Taipei, Taiwan . . . . .	Research & development, sales & marketing	67,100
Seoul, Korea . . . . .	Research & development, sales & marketing	52,500
Shanghai, China . . . . .	Research & development, sales & marketing	24,000
Shenzhen, China . . . . .	Sales & marketing	21,400
Milpitas, California . . . . .	Sales & marketing, management	13,300
Others <sup>(1)</sup> . . . . .	Sales & marketing, management	16,800

(1) Hong Kong, Macau, Yokohama, Japan, Beijing, Nanjing, Hangzhou, China

Leases covering our currently occupied leased facilities expire at varying dates, generally within the next five years. We anticipate no difficulty in retaining occupancy through lease renewals, month-to-month occupancy or replacing the leased facilities with equivalent facilities.

We currently own commercial property in Taipei of approximately 6,200 square feet, which we have no plans to use for our operations. We are in the process of selling the Taipei property. In 2017, we sold office facilities located in Shanghai, China and recognized gain from disposal of US\$1.9 million.

## Government Regulation

See Risk Factors — “We face substantial political risks associated with doing business in Taiwan because of the tense political relationship between Taiwan and the People’s Republic of China,” “We face substantial political risk associated from doing business in South Korea because of tensions in the political relationship between South Korea and North Korea,” and “Our business depends on the support of the Taiwanese and South Korean governments, and a decrease in this support may increase our tax liabilities and decrease our net income” in Item 3 above.

### ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

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

#### *General Information*

We are a global leader and pioneer in developing NAND flash controller ICs for solid-state storage devices. We supply more NAND flash controllers than any other company in the world and have one of the broadest portfolios of controller solutions and technologies. Our key products are controllers used in embedded storage products such as SSDs and eMMCs, as well as in expandable storage products such as memory cards and USB flash drives. Our products are widely used in computing and mobile devices and for industrial, enterprise, commercial and other applications. Our customers include most of the NAND flash makers, leading technology OEMs, and the majority of storage device module makers. More NAND flash products, especially next-generation flash, produced by Intel, Micron, Samsung, SK Hynix, Toshiba and Western Digital are supported by Silicon Motion controllers than any other company. We are the world’s leading merchant supplier of controllers for eMMC embedded memory used in smartphones and tablets, and the leading merchant supplier of controllers

for client SSDs used in PCs and other applications. We also supply customized specialty SSD solutions for the Chinese hyperscale data center market and for high-performance industrial applications. We market our controllers under the “SMI” brand, our enterprise-grade SSDs under the “Shannon” brand, our single-chip industrial-grade SSDs under the “Ferri SSD” and “Ferri-eMMC” brands, specially RF ICs under the “FCI” brand, and software-defined storage under the “Bigtera” brand.

Our revenue growth and product mix have been constantly evolving due to continued technological advancement of solid state storage solutions using NAND flash and demands from new applications. Historically, controllers for expandable storage products provided the majority of our revenue. Recently, a growing portion of our revenue growth has come from embedded storage products. In 2014, our embedded storage product sales accounted for over half our total sales and exceeded the sales of our expandable storage products. In 2016 and 2017, our embedded storage product sales grew to account for almost 80% and 80% of our total sales, respectively. We believe that over the next few years, as the market for embedded storage products further expands, our revenue from these new growth products, specifically client SSD controllers, will increase further. We continue to focus on adapting our business to the changing end-markets for NAND flash memory and aligning our resources accordingly. We have no assurance that our embedded storage products sales will grow consistently over the next few years, or at all.

*The following discussion of our financial condition and results of operations is based upon and should be read in conjunction with our consolidated financial statements and their related notes included in this annual report. This discussion contains forward-looking statements that involve risks and uncertainties. We caution you that our business and financial performance are subject to substantial risks and uncertainties. Actual results could differ materially from those projected in the forward-looking statements. See “Special Note Regarding Forward-Looking Statements.” In evaluating our business, you should also carefully consider the information provided under the caption “Risk Factors” included in Item 3 of this annual report.*

### **Principal Factors Affecting Our Results of Operations**

*Net sales.* Our net sales consist primarily of sales of our products, after deducting sales discounts and allowances for returns. The products that we sell are primarily for mobile storage and mobile communications markets. Net sales generated by our products by market segments for the periods indicated are as follows:

	Year Ended December 31,					
	2015		2016		2017	
	US\$	%	US\$	%	US\$	%
	(in thousands, except percentage data)					
<b>Net Sales</b>						
Mobile Storage <sup>(1)</sup> . . . . .	302,910	84	510,687	92	480,735	92
Mobile Communications <sup>(2)</sup> . . . . .	50,896	14	39,322	7	37,447	7
Others <sup>(3)</sup> . . . . .	7,491	2	6,137	1	5,222	1
<b>Total</b> . . . . .	<u>361,297</u>	<u>100</u>	<u>556,146</u>	<u>100</u>	<u>523,404</u>	<u>100</u>

(1) Includes embedded storage and expandable storage products.

(2) Includes mobile TV SoCs and handset RF ICs.

(3) Includes embedded graphics processors, demo boards, and non-recurring engineering income.



For the years ended December 31, 2015, 2016 and 2017 we derived approximately 11%, 11%, and 8%, respectively, of our net sales from customers located in the United States. We anticipate that a majority of our net sales will continue to come from customers located outside of the United States. The percentages of our net sales by geographic area for the periods indicated were as follows:

	<u>Year Ended December 31,</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
<b>Country</b>			
Taiwan .....	20%	14%	14%
Korea .....	42%	33%	34%
China .....	19%	27%	24%
United States .....	11%	11%	8%
Others .....	8%	15%	20%

Our net sales are denominated primarily in U.S. dollars. The percentages of our net sales by currency for the periods indicated are set forth in the following table:

	<u>Year Ended December 31,</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
<b>Currency</b>			
U.S. dollars .....	89%	92%	87%
Korean won .....	8%	3%	3%
Japanese yen .....	1%	—	—
Chinese yuan .....	2%	5%	10%

The length of our sales cycle, from the day purchase orders are received until products are shipped to customers, is dependent on the availability of our product inventories. If we do not have sufficient inventories on hand to meet customer demands, approximately three months are generally required from the day purchase orders are received until finished goods are manufactured and shipped to customers. This cycle can take up to six months during times when capacity at independent foundries is being fully utilized. The potential delays inherent in the manufacturing process increase the risk that we may not be able to fulfill a customer's order on time. All of our sales are made by purchase orders. Because our practice, which is consistent with industry practice, allows customers to reschedule orders on relatively short notice, order backlog may not be a good indicator of our future sales.

Because many of our semiconductor solutions are designed for the mobile and computing devices markets, we expect our business to be subject to seasonality, with higher net sales generally in the second half of each year, when customers place orders to meet increased demand during year-end holiday seasons. However, our rapid sales growth and changing product mix in recent years could make assessment of the impact of seasonal factors on our business difficult.

*Cost of sales.* Our cost of sales consists primarily of the following costs:

- cost of wafer fabrication;
- assembly, testing and shipping costs of our semiconductors;
- personnel and equipment costs associated with manufacturing support;
- quality assurance;
- cost of raw materials; and
- write-down of inventory.

We engage independent foundries for the manufacturing and processing of our semiconductors. Our manufacturing cost is subject to the cyclical supply and demand conditions typical of the semiconductor industry. Our cost per wafer generally fluctuates with the availability of capacity at independent foundries. We believe that our cost of sales is substantially variable in nature.

*Research and development expenses.* Our research and development expenses consist primarily of employee salaries and related costs, stock-based compensation expense, fees paid for the use of intellectual properties and design tools developed by third parties, development cost of software, expenses for the design, development and testing of system architecture, new product or product alternatives, costs for the construction of prototypes, occupancy costs and depreciation on research and development related equipment. We expense research and development expenditures as they are incurred.

*Sales and marketing expenses.* Our sales and marketing expenses consist primarily of employee salaries and related costs, stock-based compensation expense, commissions paid to independent distributors and costs for our advertising and promotional activities.

*General and administrative expenses.* Our general and administrative expenses consist primarily of employee salaries and related costs, stock-based compensation expense, insurance premiums, professional fees and allowance for doubtful accounts.

*Impairment of goodwill.* We evaluate the recoverability of goodwill annually, or sooner if events or changes in circumstances indicate that the carrying amount may not be recoverable.

*Amortization of acquired intangible assets.* Amortization of acquired intangible assets relates to intangible assets, such as development technology, but excluding goodwill.

*Gain from disposal of noncurrent assets held for sale.* We sold an office building which was classified as noncurrent assets held for sale and recognized the gain from disposal.

*Accounting for stock-based compensation.* We grant both stock options and restricted stock units to our employees and members of the Board of Directors. The value of our restricted stock units is expensed over the vesting period and based on the grant date share price, less the present value of expected dividends during the vesting period, discounted at a risk-free interest rate. We estimate the fair value of stock options on the date of grant using the Black-Scholes option-pricing model and recognize stock compensation expense over the requisite service period of the individual grantees, which generally equals the vesting period.

*Non-operating income and expenses.* Our non-operating income and expenses include gains or losses on the sales of investments, interest from deposited cash or short-term investments, gains or losses on foreign exchange rates, impairment of long-term investments, interest paid on loans and capital leases and other non-operating income and expenses not categorized above. We conduct an assessment on the value of our long-term investments quarterly and make corresponding write-downs as required to the value of the long-term investments.

*Provision for income taxes.* We must make certain estimates and judgments in determining income tax expenses for financial statement purposes. These estimates and judgments occur in the calculation of tax credits, benefits, deductions and allowance, and in the calculation of certain tax assets and liabilities, which arise from differences in the timing of recognition of revenue and expense for tax and financial statement purposes, as well as the interest and penalties related to uncertain tax positions.

We have operations in several countries, which include Taiwan, China and Korea, and determine income taxes for each of the jurisdictions where we operate.

In Taiwan, we have received tax exemptions from the government that are valid for a number of years and for certain income streams relating to the expansion of production capacity or the development of new technologies. The last tax credit granted to us by the Taiwanese government expired at the end of 2016. We also receive significant amounts of tax credits for applicable research and development expenses incurred in Korea. Because of these and other tax benefits, the effective tax rates of our Taiwan and Korea operations have been lower than statutory tax rates. See “Risk Factors — Our business depends on the support of the Taiwanese and South Korean governments, and a decrease in this support may increase our tax liabilities and decrease our net income” for the risks relating to our ability to enjoy favorable tax policies of the Taiwanese and Korean governments.

### **Critical Accounting Policies and Estimates**

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 on-going basis, including those related to product returns and pricing allowances, allowances for doubtful accounts, inventories, business combinations, goodwill, long-lived assets, income taxes, litigation and contingencies. 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 consolidated statements.

*Revenue recognition.* Revenue from product sales are generally recognized upon shipment to the customer provided that we have received a signed purchase order, the price has been fixed or is determinable, transfer of title has occurred in accordance with the shipping terms specified in the arrangement with the customer, collectability from the customer is considered reasonably assured, product returns are reasonably estimable and there are no remaining significant obligations or customer acceptance requirements. Revenue on development service orders is generally recognized upon completion and customer acceptance of contractually agreed milestones.

We record reserves to cover the estimated returns from our customers. Certain of our distributors have limited rights of return and price protection rights on unsold inventory. The return rights are generally limited to five percent of the monetary value of products purchased within the preceding six months to three years, provided the distributor places a corresponding restocking order of equal or greater value. The allowance for sales returns for distributors and all customers is recorded at the time of sale based on historical returns information available, management’s judgment and any known factors at the time the financial statements are prepared that would significantly affect the allowance. However, because of the inherent nature of estimates,

actual returns and allowances could be significantly different from our estimates. To the extent rates of return change, our estimates for the reserves necessary to cover such returns would also change which could have a negative impact on our recorded revenue and gross margin. We reserved approximately US\$1.8 million, US\$3.3 million and US\$3.1 million in 2015, 2016 and 2017, respectively, for estimated sales returns and discounts, representing approximately 0.5%, 0.6% and 0.6% of our gross sales for those respective periods.

Occasionally, we have reduced our product pricing due to market conditions, competitive considerations and other factors. Price protection rights are granted to certain distributors under our distribution agreements. When we reduce the price of our products, price protection allows the distributor to claim a credit against its outstanding accounts receivable balances based on the new price of the inventory it has on hand as of the date of the price reduction. A reserve for price adjustments is recorded at the time of sale based on our historical experience. The amount of our reserve for price adjustments to distributors is minimal.

*Allowance for doubtful accounts.* We record an allowance for doubtful accounts based on our evaluation of the collectability of our accounts receivable. Normal payment terms are provided to customers and applied upon transfer of title. On an ongoing basis, we analyze the payment history of customer accounts, including recent customer purchases. In circumstances where we are aware of a specific customer's inability to meet its financial obligations to us, we record a specific allowance against amounts due to reduce the net recognized receivable to the amount we reasonably believe will be collected. For all other accounts receivable due from customers, we categorize accounts receivable and make provisions based on a percentage of each category. We determine these percentages by examining our historical collection experience and current trends in the credit quality of our customers as well as our internal credit policies. If the financial condition of our customers or economic conditions in general were to deteriorate, additional allowances may be required in the future and such additional allowances would increase our operating expenses and therefore reduce our operating income and net income.

Our allowance for trade-related doubtful accounts were approximately US\$0.8 million, US\$0.7 million and US\$0.6 million as of December 31, 2015, 2016 and 2017, respectively, representing approximately 1.3%, 1.0% and 0.7% of our gross accounts receivables at the end of each respective periods.

*Inventory valuation.* We value inventories at the lower of cost or market value. Inventories are recorded at standard cost and adjusted to the approximate weighted-average cost at the balance sheet date. Market value represents the current replacement cost for raw materials, finished goods and work in process. We write down our inventory for estimated obsolescence or unmarketable inventory in an amount equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those we projected, additional inventory write-downs may be required. Inventory impairment charges establish a new cost basis for inventory and charges are not subsequently reversed to income even if circumstances later suggest that increased carrying amounts are recoverable. In estimating our reserves for obsolescence, we primarily evaluate estimates based on the timing of the introduction of our new products and the quantities remaining of our old products and write down the value of inventory on hand in excess of the estimated demand. We wrote down US\$2.5 million, US\$3.0 million and US\$0.7 million in 2015, 2016 and 2017, respectively, for estimated obsolete or unmarketable inventory.

*Valuation of long-lived assets and intangible assets with finite useful life.* We evaluate the recoverability of long-lived assets and intangible 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 sum of the anticipated undiscounted cash flows from such asset is separately identifiable and is less than the carrying value. If impairment occurs, a loss based on the excess of carrying value over the fair market value of the long-lived asset is recognized. Fair market value is determined by reference to quoted market prices, if available, or discounted cash flows, as appropriate. The impairment evaluations and the estimate of fair market value involve management estimates of assets' useful lives and future cash flows. Actual useful lives and cash flows could be different from those estimated by management. This could have a material effect on our operating results and financial condition. No impairment losses were recognized in 2015, 2016 and 2017.

*Impairment of long-term investments.* We evaluate the recoverability of long-term investments whenever events or changes in circumstances indicate the carrying value may not be recoverable. Impairment charges are determined based on the difference between our carrying value and our proportionate ownership of the investee company's fair value at year end. In 2016 and 2017, we recognized long term investments impairment of US\$13 thousand and US\$120 thousand, respectively, as a result of recurring operating losses and reduced forecasts of the investee companies which indicated that our investments were not recoverable within a reasonable period of time.

*Business combinations.* When we acquire businesses, we allocate the purchase price to tangible assets and liabilities and identifiable intangible assets acquired. Any residual purchase price is recorded as goodwill. The allocation of the purchase price requires management to make significant estimates in determining the fair values of assets acquired and liabilities assumed, especially with respect to intangible assets. These estimates are based on historical experience and information obtained from the management of the acquired companies. These estimates can include, but are not limited to, the cash flows that an asset is expected to generate in the future, the appropriate weighted-average cost of capital, and the synergistic benefits expected to be derived from the acquired business. These estimates are inherently uncertain and unpredictable. In addition, unanticipated events and circumstances may occur which may affect the accuracy or validity of such estimates.

*Goodwill.* We record goodwill when the consideration paid for an acquisition exceeds the fair value of net tangible and intangible assets acquired.

We measure and test goodwill on an annual basis or more frequently if we believe indicators of impairment exist. Our impairment review process compares the fair value of the reporting unit in which the goodwill resides to its carrying value. We determined that our reporting units are equivalent to our operating segments or components of an operating segment for the purposes of completing our impairment test. Prior to fiscal 2017, we utilize a two-step approach to testing goodwill for impairment. The first step tests for possible impairment by applying a fair value-based test. In computing fair value of our reporting units, we use estimates of future revenues, costs and cash flows from such units. The second step, if necessary, measures the amount of such impairment by comparing the implied fair value of goodwill to its carrying value. If the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recognized equal to that excess. In 2017, we elected to early adopt this ASU in the fourth quarter of 2017, in conjunction with our annual review for impairment. Estimating fair value is performed by utilizing various valuation approaches, such as income approach or market approach. The total of all reporting unit fair values was also compared to our market capitalization plus control premium for reasonableness.

In 2015 and 2016, no impairment charges were recorded. In 2017, we recorded an impairment charge of US\$10.3 million because the carrying value of the mobile communication reporting unit exceeded its fair value. The impairment charge was mainly attributable to a new project cancellation by a customer and delayed commercialization of a new product. The estimate of cash flow was based upon, among other things, certain assumptions about expected future operating performance such as revenue growth rates and operating margins used to calculate projected future cash flows, risk-adjusted discount rates, future economic and market conditions, and determination of appropriate market comparables. We based our fair value estimates on assumptions we believed to be reasonable but that are unpredictable and inherently uncertain. The long-term financial forecast represented the best estimate that we had at that time and we believed that its underlying assumptions were reasonable. However, actual performance in the near-term and longer-term could be materially different from the forecast, which could impact future estimates of fair value of our reporting units and may result in a charge to earnings in future periods due to the potential for further write-down of goodwill in connection with future impairment tests.

*Accounting for income taxes.* In preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. We are tax resident in numerous taxing jurisdictions around the world and have identified our major tax jurisdictions as Taiwan, Hong Kong, Korea and



China with statutory tax rate of 17%, 16.5%, 21.52% and 25%, respectively. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income within the relevant jurisdiction and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. The total amount of valuation allowance as of December 31, 2015, 2016 and 2017 was US\$19.0 million, US\$20.8 million and US\$19.1 million, respectively. We provide for a valuation allowance to the extent we believe that it is more likely than not that the deferred tax assets will not be recovered from future taxable income. Realization of the future tax benefits related to the deferred tax assets is dependent on many factors, including our ability to generate taxable income within the period during which the temporary differences reverse, the outlook for the economic environment in which we operate, and the overall future industry outlook. Should we determine that we would not be able to realize all or part of our net deferred tax asset in the future, an additional allowance for the deferred tax asset would be charged to income in the period the determination was made.

We utilize 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. The total amount of unrecognized tax benefits as of December 31, 2015, 2016 and 2017 was US\$5.6 million, US\$10.3 million and US\$15.1 million, respectively. As of December 31, 2016 and 2017, US\$2.6 million and US\$3.4 million, respectively, of interest and penalties were accrued. Fiscal years 2012 through 2017 remain subject to examination by the US Internal Revenue Service and other foreign tax jurisdictions. The ultimate outcome of tax matters may differ from our estimates and assumptions. Unfavorable settlement of any particular issue would require the use of cash and could result in increased income tax expense. Favorable resolution could result in reduced income tax expense. Within the next 12 months, we do not expect that our unrecognized tax benefits would change significantly. See Note 15 to the Consolidated Financial Statements for further information regarding changes in unrecognized tax benefits during 2017.

*Legal Contingencies.* From time to time, we are involved in legal actions or other third-party assertions arising in the ordinary course of business. There can be no assurance these actions or other third-party assertions will be resolved without costly litigation, in a manner that does not adversely impact our financial position, results of operations or cash flows or without requiring royalty payments in the future, which may adversely impact gross margins. We record a liability when it is probable that a loss has been incurred and the amount can be reasonably estimated. In determining the probability of a loss and consequently, determining a reasonable estimate, management is required to use significant judgment. Given the uncertainties associated with any litigation, the actual outcome can be different than our estimates and could adversely affect our results of operations, financial position and cash flows. See Item 8: "Legal Proceedings".

## Results of Operations

The following table sets forth our statements of operations as a percentage of net sales for the periods indicated:

	Year Ended December 31,		
	2015	2016	2017
Net sales	100.0%	100.0%	100.0%
Cost of sales	48.9	50.6	52.0
Gross profit	51.1	49.4	48.0
Operating expenses:			
Research and development	19.7	16.6	19.5
Sales and marketing	5.6	4.6	4.9
General and administrative	4.3	3.1	3.2
Impairment of goodwill	—	—	2.0
Amortization of intangible assets	0.3	0.4	0.5
Gain from disposal of noncurrent assets held for sale	—	—	(0.4)
Total operating expenses	29.9	24.7	29.7
Operating income	21.2	24.7	18.3
Non-operating income (expenses):			
Gain from disposal of short-term investments	0.0	0.0	0.0
Interest income	0.5	0.3	0.8
Foreign exchange gain (loss), net	0.0	(0.1)	(0.0)
Impairment of long-term investments	—	(0.0)	(0.0)
Interest expense	(0.0)	(0.0)	(0.1)
Other income (loss), net	0.0	0.0	(0.0)
Total non-operating income	0.5	0.2	0.7
Income before income taxes	21.7	24.9	19.0
Income tax expense	5.0	5.0	4.6
Net income	16.7%	19.9%	14.4%

### Comparison of Year Ended December 31, 2017 to Year Ended December 31, 2016

Net sales.

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
<b>Net sales</b>						
Mobile storage	510,687	92	480,735	92	(29,952)	(6)
Mobile communications	39,322	7	37,447	7	(1,875)	(5)
Others	6,137	1	5,222	1	(915)	(15)
Net sales	556,146	100	523,404	100	(32,742)	(6)

Our net sales decreased 6% year-over-year to approximately US\$523.4 million in 2017, primarily because of decreasing sales of products to the mobile storage market.

Our mobile storage revenue decreased 6% year-over-year primarily because of increasing sales of SSD solutions more than offset by declining eMMC, SSD and expandable storage controller sales. Mobile communications revenue decreased 5% primarily because increasing sales of mobile TV SoCs were more than offset by declining sales of CDMA transceivers, which have reached obsolescence.

*Gross profit.*

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
(in thousands, except percentage data)						
Gross profit . . . . .	274,605	49	251,194	48	(23,411)	(9)

Gross profit as a percentage of net sales decreased to 48% in 2017 as compared to 49% in 2016 primarily because of increasing sales of lower gross margin SSD solutions and declining sales of higher gross margin SSD controllers. Our gross profit excluding obsolete and unmarketable inventory write-downs as a percentage of revenue decreased from 50% in 2016 to 48% in 2017.

*Research and development expenses.*

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
(in thousands, except percentage data)						
Salary and benefits . . . . .	50,925	9	54,019	10	3,094	6
Stock-based compensation . . . . .	10,529	2	9,255	2	(1,274)	(12)
Other research and development . . . . .	30,951	6	38,779	8	7,828	25
Research and development . . . . .	92,405	17	102,053	20	9,648	10

Our research and development expenses increased 10% year-over-year to approximately US\$102.1 million in 2017. Salary and benefits increased 6% year-over-year to approximately US\$54.0 million, primarily because of more headcount in 2017. Stock-based compensation decreased 12% year-over-year to approximately US\$9.3 million. Other research and development expenses increased 25% year-over-year to approximately US\$38.8 million, primarily because of higher IC tape-out and other project expenses in 2017.

*Sales and marketing expenses.*

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
(in thousands, except percentage data)						
Salary and benefits . . . . .	15,100	3	14,425	3	(675)	(4)
Stock-based compensation . . . . .	3,122	1	3,167	1	45	1
Other sales and marketing . . . . .	7,543	1	8,276	1	733	10
Sales and marketing . . . . .	25,765	5	25,868	5	103	0

Our sales and marketing expenses increased 0% year-over-year to approximately US\$25.9 million in 2017. Salary and benefits decreased 4% year-over-year to approximately US\$14.4 million, primarily because of lower bonus payments in 2017. Stock-based compensation increased 1% year-over-year to approximately US\$3.2 million in 2017. Other sales and marketing expenses increased 10% year-over-year to approximately US\$8.3 million primarily because of more product testing fees in 2017.

*General and administrative expenses.*

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Salary and benefits . . . . .	9,184	2	9,386	2	202	2
Stock-based compensation . . . . .	3,313	—	2,779	—	(534)	(16)
Other general and administrative . . . . .	4,575	1	4,768	1	193	4
General and administrative . . . . .	17,072	3	16,933	3	(139)	(1)

Our general and administrative expenses decreased 1% year-over-year to approximately US\$16.9 million in 2017. Salary and benefits increased 2% year-over-year to approximately US\$9.4 million, primarily because of more headcount in 2017. Stock-based compensation decreased 16% year-over-year to approximately US\$2.8 million in 2017. Other general and administrative expenses increased 4% year-over-year to approximately US\$4.8 million primarily because of more professional service fees in 2017.

*Stock-based compensation.*

The following table presents details of total stock-based compensation expense that is included in each functional line item in our consolidated statements of income:

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Cost of sales . . . . .	400	—	293	—	(107)	(27)
Research and development . . . . .	10,529	2	9,255	2	(1,274)	(12)
Sales and marketing . . . . .	3,122	1	3,167	1	45	1
General and administrative . . . . .	3,313	—	2,779	—	(534)	(16)
Total stock-based compensation . . . . .	17,364	3	15,494	3	(1,870)	(11)

Total stock-based compensation, all of which are RSU expenses, decreased 11% in 2017.

See Note 17 to Consolidated Financial Statements for a discussion of activity related to share-based awards.

*Impairment of goodwill.* We performed annual impairment assessments of the carrying value of goodwill in November 2016 and 2017. No impairment was recognized in 2016. During our 2017 evaluation, we compared the carrying value of FCI to its estimated fair value and determined that goodwill was impaired and recognized approximately US\$10.3 million for goodwill impairment.

*Amortization of intangible assets.*

	Years Ended December 31					
	2016		2017		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Amortization of intangible assets . . . . .	2,103	—	2,534	—	431	20

Our amortization of intangible asset increased 20% year-over-year to approximately US\$2.5 million because of our acquisition of Bigtera in July 2017.

*Gain (loss) from disposal of noncurrent assets held for sale.* In 2017, we sold an office building located in Shanghai, China and recognized a gain from disposal of US\$1.9 million.

*Gain from disposal of short-term investments.* We realized gains on sales of the trading securities of US\$2 thousand and US\$103 thousand for the years ended December 31, 2016 and 2017, respectively.

*Interest income.* Our interest income increased to approximately US\$4.3 million for the year ended December 31, 2017 from approximately US\$2.2 million for the year ended December 31, 2016.

*Impairment of long-term investment.* In 2016 and 2017, we determined that our investments in Cashido and Vastview were impaired because a combination of recurring losses and reduced forecasts indicated that our investments were not recoverable within a reasonable period of time and that the impairments were other than temporary and recorded a combined impairment charge of US\$13 thousand and US\$120 thousand, respectively.

*Interest expense.* Our interest expense increased to approximately US\$423 thousand for the year ended December 31, 2017 from approximately US\$127 thousand for the year ended December 31, 2016 because of greater use of bank credit facilities.

*Foreign exchange gain (loss), net.* For the year ended December 31, 2017, we incurred foreign exchange losses of US\$157 thousand, compared with US\$692 thousand for the year ended December 31, 2016. We do not engage in any hedging activities.

*Income tax expense (benefit).* Our income tax expense was approximately US\$24.0 million for the year ended December 31, 2017 compared to an income tax expense of approximately US\$27.7 million for the year ended December 31, 2016.

*Net income (loss).* Net income was approximately US\$75.0 million for the year ended December 31, 2017 compared to a net income of approximately US\$110.9 million for the year ended December 31, 2016.

### **Comparison of Year Ended December 31, 2016 to Year Ended December 31, 2015**

*Net sales.*

	Years Ended December 31					
	2015		2016		US\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
<b>Net sales</b>						
Mobile storage	302,910	84	510,687	92	207,777	69
Mobile communications	50,896	14	39,322	7	(11,574)	(23)
Others	7,491	2	6,137	1	(1,354)	(18)
Net sales	361,297	100	556,146	100	194,849	54

Our net sales increased 54% year-over-year to approximately US\$556.1 million in 2016, primarily because of increasing sales of products to the mobile storage market.

Our mobile storage revenue increased 69% year-over-year primarily because of increasing sales of eMMC and SSD controllers and SSD solutions, partially offset by declining expandable storage controller sales. Mobile communications revenue decreased 23% primarily because of decreasing mobile TV SoC and LTE transceiver sales.



*Gross profit.*

	Years Ended December 31					
	2015		2016		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Gross profit	184,532	51	274,605	49	90,073	49

Gross profit as a percentage of net sales decreased to 49% in 2016 as compared to 2015 primarily because of lower gross margin mobile storage and mobile communications sales. Our gross profit excluding obsolete and unmarketable inventory write-downs as a percentage of revenue decreased from 52% in 2015 to 50% in 2016.

*Research and development expenses.*

	Years Ended December 31					
	2015		2016		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Salary and benefits	39,925	11	50,925	9	11,000	28
Stock-based compensation	6,565	2	10,529	2	3,964	60
Other research and development	24,671	7	30,951	6	6,280	25
Research and development	71,161	20	92,405	17	21,244	30

Our research and development expenses increased 30% year-over-year to approximately US\$92.4 million in 2016. Salary and benefits increased 28% year-over-year to approximately US\$50.9 million, primarily because of more headcount and compensation expenses in 2016. Stock-based compensation increased 60% year-over-year to approximately US\$10.5 million. Other research and development expenses increased 25% year-over-year to approximately US\$31.0 million, primarily because of higher IC tape-out and other project expenses in 2016.

*Sales and marketing expenses.*

	Years Ended December 31					
	2015		2016		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Salary and benefits	12,494	3	15,100	3	2,606	21
Stock-based compensation	1,790	1	3,122	1	1,332	74
Other sales and marketing	5,889	2	7,543	1	1,654	(14)
Sales and marketing	20,173	6	25,765	5	5,592	28

Our sales and marketing expenses increased 28% year-over-year to approximately US\$25.8 million in 2016. Salary and benefits increased 21% year-over-year to approximately US\$15.1 million, primarily because of more headcount and compensation expenses in 2016. Stock-based compensation increased 74% year-over-year to approximately US\$3.1 million in 2016. Other sales and marketing expenses increased 28% year-over-year to approximately US\$7.5 million primarily because of more commission expenses in 2016.

*General and administrative expenses.*

	Years Ended December 31					
	2015		2016		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Salary and benefits . . . . .	8,568	2	9,184	2	616	7
Stock-based compensation . . . . .	1,802	1	3,313	—	1,511	84
Other general and administrative . . . . .	5,344	1	4,575	1	(769)	(14)
General and administrative . . . . .	15,714	4	17,072	3	1,358	9

Our general and administrative expenses increased 9% year-over-year to approximately US\$17.1 million in 2016. Salary and benefits increased 7% year-over-year to approximately US\$9.2 million, primarily because of more headcount and compensation expenses in 2016. Stock-based compensation increased 84% year-over-year to approximately US\$3.3 million in 2016. Other general and administrative expenses decreased 14% year-over-year to approximately US\$4.6 million primarily because of lower professional service expenditures in 2016.

*Stock-based compensation.*

The following table presents details of total stock-based compensation expense that is included in each functional line item in our consolidated statements of income:

	Years Ended December 31					
	2015		2016		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Cost of sales . . . . .	261	—	400	—	139	53
Research and development . . . . .	6,565	2	10,529	2	3,964	60
Sales and marketing . . . . .	1,790	1	3,122	1	1,332	74
General and administrative . . . . .	1,802	1	3,313	—	1,511	84
Total stock-based compensation . . . . .	10,418	4	17,364	3	6,946	67

Total stock-based compensation, all of which are RSU expenses, increased 67% in 2016.

See Note 17 of Notes to Consolidated Financial Statements for a discussion of activity related to share-based awards.

*Amortization of intangible assets.*

	Years Ended December 31					
	2015		2016		\$ change	% change
	US\$	% of net sales	US\$	% of net sales		
	(in thousands, except percentage data)					
Amortization of intangible assets . . . . .	1,051	—	2,103	—	1,052	100

Our amortization of intangible asset increased 100% year-over-year to approximately US\$2.1 million because of our acquisitions of Shannon Systems in July 2015.

*Gain from disposal of short-term investments.* We realized gains on sales of the trading securities US\$3 thousand and US\$2 thousand for the years ended December 31, 2015 and 2016, respectively.

*Interest income.* Our interest income increased to approximately US\$2.2 million for the year ended December 31, 2016 from approximately US\$2.0 million for the year ended December 31, 2015.

*Impairment of long-term investment.* No impairment was recognized in 2015. In 2016, we determined that our investments in Cashido were impaired because a combination of recurring losses and reduced forecasts indicated that our investments were not recoverable within a reasonable period of time and that the impairments were other than temporary and recorded a combined impairment charge of US\$13 thousand.

*Interest expense.* Our interest expense increased to approximately US\$127 thousand for the year ended December 31, 2016 from approximately US\$47 thousand for the year ended December 31, 2015 because of greater use of bank credit facilities.

*Foreign exchange gain (loss), net.* For the year ended December 31, 2016, we had a foreign exchange loss of approximately US\$0.7 million compared to the foreign exchange gain of less than US\$0.1 million for the year ended December 31, 2015. We do not engage in any hedging activities.

*Income tax expense (benefit).* Our income tax expense was approximately US\$27.7 million for the year ended December 31, 2016 compared to an income tax expense of approximately US\$18.2 million for the year ended December 31, 2015.

*Net income (loss).* Net income was approximately US\$110.9 million for the year ended December 31, 2016 compared to a net income of approximately US\$60.3 million for the year ended December 31, 2015.

## Liquidity and Capital Resources

As of December 31, 2017, we had approximately US\$359.5 million in cash and cash equivalents and approximately US\$6.9 million in short-term investments. We maintain our cash balances in bank deposits and in money market instruments. We do not engage in any currency hedging activities. Our short-term investments consist primarily of bond funds and principal protected notes that we trade.

We believe our existing cash balances and short-term investments, together with cash we expect to generate from operating activities, will be sufficient to meet our anticipated cash needs for at least the next 12 months. Our future capital requirements will depend on many factors, including the level of our net sales, the timing and extent of spending to support product development efforts, the expansion of sales and marketing activities, the timing of introductions of new products, the costs to ensure access to adequate manufacturing capacity, the continuing market acceptance of our products, availability of attractive acquisition and investment opportunities, dividend payments, and share repurchases. We could be required, or could elect, to seek additional funding through public or private equity or debt financing, and additional funds may not be available on terms acceptable to us or at all.

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

	Year Ended December 31,		
	2015	2016	2017
As Adjusted <sup>(1)</sup>	US\$	US\$	US\$
	(in thousands)		
<b>Consolidated Cash Flow Data:</b>			
Net cash provided by operating activities . . . . .	65,946	125,568	103,881
Net cash used in investing activities <sup>(1)</sup> . . . . .	(58,458)	(8,220)	(14,548)
Net cash provided by (used in) financing activities . . .	(20,271)	2,194	(31,740)
Depreciation and amortization . . . . .	8,987	11,585	13,133
Capital expenditures . . . . .	(23,664)	(12,220)	(11,683)

- (1) The selected consolidated statement of cash flow data for the year ended December 31, 2015 was retrospectively adjusted to reflect the Company's election to early adopt the accounting update of the classification and presentation of changes in restricted cash on the statement of cash flows. See Note 2 to our audited consolidated financial statement included in this annual report for more information.

### ***Operating activities***

Our net cash provided by operating activities was approximately US\$103.9 million for the year ended December 31, 2017, compared to net cash provided by operating activities of approximately US\$125.6 million and US\$65.9 million during 2016 and 2015, respectively.

For the year ended December 31, 2017, cash flow provided by operations of US\$103.9 million resulted primarily from our net income of US\$75 million and the following reasons:

- Our net income includes substantial non-cash charges, namely US\$13.1 million of depreciation and amortization and US\$15.5 million of stock-based compensation.
- We increased working capital by US\$5.6 million. Inventory increased by US\$22.3 million, notes and accounts receivable increased by US\$5.2 million, notes and accounts payable increased by US\$24.2 million, income tax payable decreased by US\$8.7 million, and other assets net of other liabilities provided US\$6.4 million of cash.

For the year ended December 31, 2016, cash flow provided by operations of US\$125.6 million resulted primarily from our net income of US\$110.9 million and the following reasons:

- Our net income includes substantial non-cash charges, namely US\$11.6 million of depreciation and amortization and US\$17.4 million of stock-based compensation.
- We increased working capital by US\$8.3 million. Inventory increased by US\$24.8 million, notes and accounts receivable increased by US\$14.6 million, notes and accounts payable increased by US\$9.2 million, income tax payable increased by US\$6.9 million, and other assets net of other liabilities provided US\$15.0 million of cash.

### ***Investing activities***

Our net cash used in investing activities was approximately US\$14.5 million for the year ended December 31, 2017, compared to net cash used in investing activities of approximately US\$8.2 million for the year ended December 31, 2016. In 2017, we paid US\$11.7 million for the routine purchase of software, design tools and other items and US\$2.9 million to acquire Bigtera.

Our net cash used in investing activities was approximately US\$8.2 million for the year ended December 31, 2016, compared to net cash used in investing activities of approximately US\$58.5 million for the year ended December 31, 2015. In 2016, we paid \$12.2 million for the routine purchase of software, design tools and other items.

### ***Financing activities***

Our net cash used in financing activities was approximately US\$31.7 million for the year ended December 31, 2017, compared to net cash provided by financing activities of approximately US\$2.2 million for the year ended December 31, 2016. Our cash used in financing activities in 2017 consists primarily of US\$32.1 million of dividend payments.

Our net cash provided by financing activities was approximately US\$2.2 million for the year ended December 31, 2016, compared to net cash used in financing activities of approximately US\$20.3 million for the year ended December 31, 2015. Our cash provided by financing activities in 2016 consists primarily of US\$25.0 million of loans from banks offset by US\$22.9 million of dividend payments.

## Contractual Obligations

The following table sets forth our commitments to settle contractual obligations in cash as of December 31, 2017:

	Amount of Commitment Maturing by Year				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
	US\$	US\$	US\$	US\$	US\$
			(in thousands)		
Operating leases . . . . .	9,546	3,711	4,611	1,224	—
Capital leases . . . . .	125	125	—	—	—
Pension . . . . .	1,768	1,768	(a)	(a)	(a)
Long-term payable . . . . .	674	566	108	—	—
Other long term liabilities . . . . .	<u>7,456</u>	<u>1,244</u>	<u>6,212</u>	<u>—</u>	<u>—</u>
Contractual cash obligations . . . . .	<u>19,569</u>	<u>7,414</u>	<u>10,931</u>	<u>1,224</u>	<u>—</u>

(a) Our pension obligation after one year has not been estimated.

We increased long-term taxes payable of US\$4,770 thousand related to uncertain tax positions as of December 31, 2017. At this time, we are unable to make a reasonably reliable estimate of the timing of payments in individual years beyond 12 months due to uncertainties in the timing and outcome of a potential tax audit.

## Off-balance Sheet Arrangements

We currently do not have any outstanding derivative financial instruments, off-balance sheet guarantees or arrangements, interest rate swap transactions, or foreign currency forward contracts. We do not engage in any trading activities involving non-exchange traded contracts.

## Recent Accounting Pronouncements

Please refer to Note 2 to the consolidated financial statements



## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### Executive Officers and Directors

Members of our board of directors are elected by our shareholders. Our board of directors consists of seven directors.

Our executive officers are appointed by, and serve at the discretion of, our board of directors. The following table sets forth information regarding our directors and executive officers as of the date of this annual report.

<u>Name</u>	<u>Age</u>	<u>Position</u>
James Chow	67	Chairman of the Board
Wallace C. Kou	59	President, Chief Executive Officer and Director
Steve Chen	46	Director
Tsung-Ming Chung	68	Director
Lien-Chun Liu	60	Director
Yung-Chien Wang	55	Director
Han-Ping D. Shieh	64	Director
Riyadh Lai	49	Chief Financial Officer
Nelson Duann	49	Senior VP of Marketing & OEM Business, Mobile Storage
Sangwoo Han	49	Senior VP and General Manager, Mobile Communications
Xueshi Yang	41	Senior VP and General Manager, Shannon Systems
Arthur Yeh	57	VP of Sales, Mobile Storage
Robert Fan	54	President of SMI USA
John (Chun-O) Kim	57	VP of Sales, Mobile Communications
David Yu	43	VP of Sales & Marketing, Shannon Systems
Leander Yu	43	VP of Sales & Marketing, Bigtera
Frank Chang	51	VP of R&D, Mobile Storage
Ken Chen	56	VP of Operations
Kevin Yeh	54	VP of R&D, Algorithm & Technology
John (Jong Ryul) Lee	54	VP of R&D, Mobile Communications
Derek Zhou	41	VP of R&D, Shannon Systems
Jason Chiang	50	VP of HR and Administration, and Special Assistant to CEO
Frank Shu	61	VP of R&D, Verification Engineering & Compatibility Test
Mike Jing	58	VP of IT

### Executive Officers and Directors

#### James Chow, Chairman of the Board of Directors

Mr. Chow has served as the Chairman of our board of directors since April 2005. Mr. Chow has been the Chairman of Concord Financial Co., Ltd. since 1993. Concord Financial Co., Ltd. is an investment holding company and was one of our significant shareholders. Mr. Chow has an MBA from Columbia University.

#### Wallace C. Kou, President, Chief Executive Officer, Director

Mr. Kou founded Silicon Motion in 1995 and has been our President and Chief Executive Officer since our founding. Prior to founding Silicon Motion, Mr. Kou was the Vice President and Chief Architect at the Multimedia Products Division of Western Digital Corporation, which developed graphics processors for notebook PCs and was sold to Philips Semiconductor in 1995. Before Western Digital, Mr. Kou worked for Wyse Technology. Mr. Kou has a BS in Electrical & Control Engineering from the National Chiao Tung University in Taiwan and an MS in Electrical & Computer Engineering from the University of California at Santa Barbara.

**Steve Chen, Director**

Mr. Chen joined our board of directors in 2012. Mr. Chen is the chairman of Mercuries Co., Ltd.. Mr. Chen has two Master of Engineering degrees from Cornell University.

**Tsung-Ming Chung, Director**

Mr. Chung joined our board of directors in June 2005. Mr. Chung is the Chairman of Dynapack International Technology Corp, a leading provider of battery packs for notebook PCs and tablets. From 1985 to 2000, Mr. Chung was an audit partner at Arthur Andersen. He is also a director at Far East International Bank and Taiwan Mobile Corporation. Mr. Chung has a BA in Business Administration from the National Taiwan University and an MBA from the National Cheng-chi University in Taiwan.

**Lien-Chun Liu, Director**

Ms. Liu joined our board of directors in June 2005. She is Vice President of the International Council of Women and currently also serves on the board of supervisors of Concord VIII Venture Capital Co., Ltd. and the board of directors of New Tamsui Golf Course. She was formerly a research fellow at the Taiwan Research Institute and served on the board of supervisors of China Television Corp. from 2000 to 2004. Ms. Liu has a BA from Wellesley College and a JD from Boston College Law School.

**Yung-Chien Wang, Director**

Mr. Wang joined our board of directors in June 2005. Mr. Wang has over 20 years of working experience in the human resource and legal services industries. Mr. Wang has been a consultant of Professional Trust Co., Ltd., a human resource consulting firm in Taiwan since August 1998 and is currently its Vice President. Mr. Wang has a law degree from Fu Jen Catholic University in Taiwan.

**Han-Ping D. Shieh, Director**

Mr. Shieh joined our board of directors in 2014. He is a Chair Professor at National Chiao Tung University (NCTU) in Taiwan, a fellow of the Institute of Electrical and Electronics Engineers, The Optical Society and the Society for Information Display and a board member of Young Optics Inc. and Focal Tech. Inc. Mr. Shieh received his PhD in Electrical and Computer Engineering from Carnegie Mellon University in 1987. He joined NCTU as a professor in 1992 and was previously a Research Staff Member at the IBM Thomas J. Watson Research Center. He was previously the Dean of the College of Electrical and Computer Engineering, Senior Vice President at NCTU and Vice Chancellor at the University of Taiwan.

**Riyadh Lai, Chief Financial Officer**

Mr. Lai joined us in April 2007 from ING Corporate Finance, Asia, where he was the Head of the Technology Group. Previously, he was also an investment banker at Morgan Stanley and ABN AMRO and finance manager at PepsiCo in Hong Kong and New York. Mr. Lai has over two decades of finance and financial management experience. He has a BA in Economics from Georgetown University and an MBA from New York University.

**Nelson Duann, Senior VP of Marketing & OEM Business, Mobile Storage**

Mr. Duann became our Senior Vice President in charge of our mobile storage marketing and OEM business in July 2015. He joined Silicon Motion in August 2007 as a product marketing director and R&D team leader. Mr. Duann has almost 20 years of experience in the semiconductor industry in product design, development and marketing. Prior to Silicon Motion, he worked for Sun Microsystems Inc., focusing on UltraSPARC microprocessor projects. He has an MS in Communications Engineering from National Chiao Tung University in Taiwan and an MS in Electrical Engineering from Stanford University.

### **Sangwoo Han, Senior VP and General Manager, Mobile Communications**

Mr. Han became the General Manager of our Mobile Communications product line in July 2008. He was formerly the Chief Technology Officer at FCI, a company that we acquired in April 2007. Mr. Han joined FCI in 2003 and had been in charge of product design, development, production and marketing. In 1997, he co-founded RF Solutions Inc. in Atlanta, Georgia, which became the Anadigics Wireless LAN Center of Excellence. Mr. Han has a BS in Electrical Engineering from Carnegie-Mellon University, an MS in Electrical Engineering from the University of Pennsylvania, and a PhD in Electrical Engineering from the Georgia Institute of Technology.

### **Xueshi Yang, Senior VP and General Manager, Shannon Systems**

Mr. Yang joined us in July 2015 as General Manager of Shannon Systems, our enterprise SSD product line, following our acquisition of this business. He co-founded Shannon Systems in 2011 and as CEO, led the development and commercialization of enterprise-grade PCIe SSDs that were the industry's first in terms of storage capacity and scalability, ultra-low latency and low-power envelope. Prior to Shannon, Mr. Yang was the chief architect at Marvell of its first generations of SSD controllers, a research staff at Seagate and postdoctoral researcher at Princeton University. He holds a PhD in Electrical Engineering from Drexel University and a BS in Electrical Engineering from Tsinghua University in China. Mr. Yang has more than 100 US patents granted or pending relating to SSDs.

### **Arthur Yeh, VP of Sales, Mobile Storage**

Mr. Yeh has served as our Vice President in charge of our mobile storage sales since November 2004. Mr. Yeh has over 20 years of sales experience managing marketing strategies, including product promotions and sales activities for semiconductor products. Mr. Yeh previously served in management positions at VIA Technologies for 10 years and joined us in 2004. Mr. Yeh holds an MS degree in Management Business Administration from the National Chung Hsing University, in Taiwan.

### **Robert Fan, President of SMI USA**

Mr. Fan has served as President of SMI USA in charge of Silicon Motion's business operations in the Americas and Europe since November 2016. He also oversees corporate marcom and PR efforts as well as the graphics business. Mr. Fan has over 25 years of sales and marketing experience and joined Silicon Motion in May 2013 as Vice President and General Manager of SMI USA. Prior to Silicon Motion, Mr. Fan served in executive management roles at Spansion, IDT, Staktek, Berkana Wireless (acquired by Qualcomm) and Resonext (acquired by RF Micro Devices). He also spent over nine years at Intel in sales, marketing and management positions. Mr. Fan holds a BS in Electrical Engineering from the University of California, Berkeley and MSEE from Santa Clara University, and completed the General Management Executive Program at McCombs School of Business, University of Texas.

### **John (Chun-O) Kim, VP of Sales, Mobile Communications**

Mr. Kim became the Vice President of our Mobile Communications product line in July 2008. He was formerly the Vice President of Sales at FCI, a company that we acquired in April 2007. Mr. Kim joined FCI in 2006 and had previously served in management positions at Hewlett-Packard's semiconductor division (which became Avago Technologies) and as a CEO of a private company. Mr. Kim has over 16 years of semiconductor sales leadership experience, including managing marketing strategies, product promotions and sales activities. He has an MS in Electrical Engineering from Ajou University in Korea.

### **David Yu, VP of Sales & Marketing, Shannon Systems**

Mr. Yu joined us in July 2015 as Vice President of Sales & Marketing of Shannon Systems, our enterprise SSD product line, following our acquisition of this business. He joined Shannon Systems in 2014 and has been

instrumental in managing its rapid sales growth. Previously and for over 10 years, he held sales leadership positions at Infineon and RF Micro Devices in China. He holds an MS in Management from the University of Ottawa and a BS in Electrical Engineering from Tsinghua University in China.

**Leander Yu, VP of Sales & Marketing, Bigtera**

Mr. Yu joined us in July 2017 as Vice President of Sales and Marketing of Bigtera, our software-defined storage (SDS) product line, following our acquisition of this business. He founded Bigtera in 2012 to provide enterprise-class SDS to the Greater China market. Prior to Bigtera, Mr. Yu was a senior architect at Trend Micro and its subsidiary TCloud Computing and responsible for the design of software solutions including cloud storage products. He has a BS in Computer Science and Information Engineering from National Taiwan University.

**Frank Chang, VP of R&D, Mobile Storage**

Mr. Chang has served as our Vice President of research and development since 2008. Mr. Chang is head of research and development for our mobile storage products and has around 20 years of experience in the integrated circuit design industry. He was previously a project manager of firmware development at Holtek Semiconductors. Mr. Chang has a BS in Electrical Engineering from the National Changhua University of Education in Taiwan.

**Ken Chen, VP of Operations**

Mr. Chen has served as our Vice President in charge of operations since November 2003. Mr. Chen has over 20 years of manufacturing and operations experience in the semiconductor industry, managing supply chain and virtual manufacturing systems including wafer fabrication, mask tooling, as well as assembly and testing. Mr. Chen previously served in management positions at Faraday Technology and UMC, and joined us in 2003. Mr. Chen has a BS in Industrial Engineering from Chung Yuan Christian University in Taiwan and an MS in Industrial Engineering and Engineering Management from the National Tsing Hua University, Taiwan.

**Kevin Yeh, VP of R&D, Algorithm & Technology**

Mr. Yeh became our Vice President of research and development in August 2012. He joined Silicon Motion in September 2003 as a product marketing director, before leading our Algorithm and Technology R&D team. Mr. Yeh has more than 20 years of experience in semiconductor product design, development and marketing. Prior to Silicon Motion, Mr. Yeh worked in Taiwan Semiconductor Manufacturing Company, Neo Magic, VLSI Technology and LSI. Mr. Yeh holds a BS degree in Control Engineering from National Chiao Tung University in Taiwan and an MS degree in Electronic Engineering from Syracuse University.

**John (Jong Ryul) Lee, VP of R&D, Mobile Communications**

Mr. Lee became the Vice President of our Mobile Communications product line in July 2008. He was formerly the Vice President of R&D at FCI, a company that we acquired in April 2007. Mr. Lee joined FCI in 2000 and had been in charge of product design, development, production and quality systems. In 2013, he became a director of the Semiconductor & Device Society of The Institute of Electronics Engineers of Korean (IEEK). He was previously a senior engineer at the Electronics and Telecommunications Research Institute (ETRI) in Korea. Mr. Lee has a BS and an MS in Electronics Engineering from Chung Ang University in Korea.

**Derek Zhou, VP of R&D, Shannon Systems**

Mr. Zhou joined us in July 2015 as Vice President of R&D of Shannon Systems, our enterprise SSD product line, following our acquisition of this business. He co-founded Shannon Systems in 2011 with Mr. Yang and as CTO, managed the development of enterprise-grade PCIe SSDs that were the industry's first in terms of storage

capacity and scalability, ultra-low latency and low-power envelope. Prior to Shannon, he was a senior ASIC design engineer with 10 years of experience at Nvidia and Chrontel. He holds an MS in Electrical Engineering from Binghamton University and a BS in Electrical Engineering from Tsinghua University in China.

### **Jason Chiang, VP of HR and Administration and Special Assistant to CEO**

Mr. Chiang joined Silicon Motion in 2002 and has been serving as our Vice President of HR and Administration and Special Assistant to our CEO since 2005. Mr. Chiang has more than 18 years of finance and business administration experience. Prior to joining Silicon Motion, Mr. Chiang was a Director at Concord Venture Capital. Mr. Chiang has a BS in Economics from the National Taiwan University and an MS in Business Administration from Rochester University.

### **Frank Shu, VP of R&D, Verification Engineering & Compatibility Test**

Mr. Shu has served as our Vice President of R&D, Verification Engineering & Compatibility Test since September 2013. He joined us in July 2012 as Vice President of SSD System Technology. Mr. Shu has more than 20 years of experience in the storage and PC system industry. Before joining Silicon Motion, Mr. Shu was the VP of R&D in charge of SSD testing at Allion Labs. Mr. Shu also worked for Microsoft and played a key role in defining and developing the software storage stack for the Windows operating system. Prior to Microsoft, Mr. Shu worked for Fujitsu, Seagate and Everex. Mr. Shu has a BS in Electronic Engineering from Nanjing Aeronautical Institute in China and an MS in Computer Science from the Oregon Graduate Institution of Science & Technology.

### **Mike Jing, VP of IT**

Mr. Jing became our Vice President of IT in August 2016. He joined Silicon Motion in January 2003 and currently leads our IT/MIS team. Prior to Silicon Motion, he worked for Teradyne. Mr. Jing has almost 30 years of experience in software development and IT management and holds a BS and MS in Computer Engineering from the National Chiao Tung University in Taiwan and an MS in Computer Science from the University of California, San Diego.

There is no arrangement or understanding 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.

## **Board Practices**

### ***Board Committees***

Our board of directors has established an audit committee, a compensation committee, and a nominating and corporate governance committee.

*Audit Committee.* The audit committee is responsible for reviewing the financial information that will be provided to shareholders and others, reviewing the systems of internal controls that management and the board of directors have established, appointing, retaining and overseeing the performance of independent registered public accounting firms, overseeing our accounting and financial reporting processes and the audits of our financial statements, and pre-approving audit and permissible non-audit services provided by independent registered public accounting firms. Tsung-Ming Chung, Lien-Chun Liu, and Yung-Chien Wang are members of our audit committee. Our board of directors has determined that Mr. Chung, the Chairman of the audit committee, is the committee's "Audit Committee Financial Expert" as required by Nasdaq and U.S. Securities and Exchange Commission ("SEC") rules.

*Compensation Committee.* The compensation committee's basic responsibility is to review the performance and development of management in achieving corporate goals and objectives and to assure that our senior executives are compensated effectively in a manner consistent with our strategy, competitive practice and the



requirements of the appropriate regulatory bodies. Toward that end, this committee oversees, reviews and administers all of our compensation, equity and employee benefit plans and programs. Lien-Chun Liu, Steve Chen, and Yung-Chien Wang are members of our compensation committee, with Mr. Chen serving as the Chairman of the committee.

*Nominating and Corporate Governance Committee.* The nominating and corporate governance committee is responsible for overseeing, reviewing and making periodic recommendations concerning our corporate governance policies, and for recommending to the full board of directors candidates for election to the board of directors. Lien-Chun Liu, Steve Chen, and Yung-Chien Wang are members of our nominating and corporate governance committee, with Ms. Liu serving as the Chairman of the committee.

Our board of directors has adopted a code of ethics, which is applicable to all of our employees. Our Code of Ethics is posted on our website at [www.siliconmotion.com](http://www.siliconmotion.com).

### **Duties of Directors**

Under Cayman Islands law, our directors have a duty to act honestly, in good faith and with a view to the best interests of our company. Our directors also have a duty to exercise the care, diligence and skills that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to our company, our directors must ensure compliance with our memorandum and articles of association. The functions and powers of our board of directors include, among others:

- convening shareholders' meetings and reporting its work to shareholders at such meetings;
- implementing shareholders' resolutions;
- determining our business plans and investment proposals;
- formulating our profit distribution plans and loss recovery plans;
- determining our debt and finance policies and proposals for the increase or decrease in our registered capital and the issuance of debentures;
- formulating our major acquisition and disposition plans, and plans for merger, division or dissolution;
- proposing amendments to our amended and restated memorandum and articles of association; and
- exercising any other powers conferred by the shareholders' meetings or under our amended and restated memorandum and articles of association.

### **Terms of Directors and Officers**

Under Cayman Islands law and our articles of association, our directors hold office until a successor has been duly elected and qualified. Our articles of association provide that our directors serve for a term of three years, with one-third of the directors (or, if their number is not a multiple of three, the number nearest to but not greater than one-third) subject to re-election at each annual general meeting of shareholders (chairman and managing director not subject to retirement by rotation nor to be taken into account in determining the number of directors to retire), unless the director was appointed by the board of directors, in which case such director holds office until the next annual meeting of shareholders at which time such director is eligible for re-election. One of our seven directors is currently subject to re-election at our next annual general meeting of shareholders. All of our executive officers are appointed by and serve at the discretion of our board of directors.

### **Limitation on Liability and Other Indemnification Matters**

Cayman Islands law and our articles of association allow us to indemnify our directors, secretary and other officers acting in relation to any of our affairs against actions, costs, charges, losses, damages and expenses

incurred by reason of any act done or omitted in the execution of their duties as our directors, secretary and other officers. Under our memorandum and articles of association, indemnification is not available to any matter in respect of any fraud, dishonesty, willful misconduct or bad faith which may attach to any of them.

### **Compensation of Directors and Executive Officers**

For the year ended December 31, 2017, the aggregate compensation to our directors and senior executive officers was approximately US\$5.05 million. In 2017, we granted options and restricted stock units to our executive officers as a group to acquire an aggregate of 233,200 ordinary shares. The options and restricted stock units granted to our executive officers and non-executive directors are subject to the same vesting conditions as those of our employees.

### **Service Contracts**

We currently do not have service contracts with our directors.

### **Share-Based Compensation Plans and Option Grants**

In April 2005, our board of directors and shareholders adopted our 2005 Incentive Plan. Our shareholders approved our Amended and Restated 2005 Incentive Plan (referred to in this report as the “2005 Plan”) at our Annual General Meeting in August 2006, including an amendment to increase the authorized number of shares available for issuance under the plan from 10,000,000 shares to 25,000,000 shares. In 2009, the board of directors amended the 2005 Plan to increase the authorized shares available for issuance under the 2005 Plan to 40,000,000 shares. The 2005 Plan expired by its terms on April 22, 2015. On June 3, 2015, the board of directors adopted the 2015 Incentive Plan (the “2015 Plan” and together with the 2005 Plan, the “Plans”). The 2015 Plan reserved 20,000,000 shares of ordinary shares for issuance upon exercise of stock options and restricted stock units. The Plans provide for the grant of stock options, stock bonuses, restricted stock awards, restricted stock units and stock appreciation rights, which may be granted to our employees (including officers), directors and consultants.

*Share Reserve.* The aggregate number of ordinary shares that may be issued pursuant to awards granted under the 2005 Plan could not exceed 40,000,000 shares and the aggregate number of ordinary shares that may be issued pursuant to awards granted under the 2015 Plan will not exceed 20,000,000, inclusive of ordinary shares issuable upon exercise of awards previously granted under the Silicon Motion, Inc. Guidelines for Issuance and Subscription of Employee Stock Option, which options we have, subject to the consent of the respective option-holders, agreed to assume in the share exchange.

The following types of shares issued under the Plans may again become available for the grant of new awards under the Plans: restricted stock issued under the Plans that is forfeited or repurchased by us prior to it becoming fully vested; shares withheld for taxes; shares tendered to us to pay the exercise price of an option; and shares subject to awards issued under the Plans that have expired or otherwise terminated without having been exercised in full.

*Administration.* The board of directors will administer the Plans and may delegate this authority to administer the plan to a committee. Subject to the terms of the Plans, the plan administrator, which is our board of directors or its authorized committee, determines recipients, grant dates, the numbers and types of stock awards to be granted and the terms and conditions of the stock awards, including the period of their exercisability and vesting. Subject to certain limitations, the plan administrator will also determine the exercise price of options granted, the purchase price for restricted stock and restricted stock units, and, if applicable, the strike price for stock appreciation rights.

*Capitalization adjustments.* In the event of a dividend or other distribution (whether in the form of cash, ordinary shares, other securities, or other property), recapitalization, stock split, reorganization, merger,

consolidation, exchange of our ordinary shares or our other securities, or other change in our corporate structure, the board of directors may adjust the number and class of shares that may be delivered under the Plans and the number, class and price of the shares covered by each outstanding stock award.

*Changes in control.* In the event of a change in control of the company, all outstanding options and other awards under the Plans may be assumed, continued or substituted for by any surviving or acquiring entity. If the surviving or acquiring entity elects not to assume, continue or substitute for such awards, the vesting of such awards held by award holders whose service with us or any of our affiliates has not terminated will be accelerated and such awards will be fully vested and exercisable immediately prior to the consummation of such transaction, and the stock awards shall automatically terminate upon consummation of such transaction if not exercised prior to such event.

*Amendments to 2005 Plan in 2009 and 2010.* In 2009, our board of directors amended the 2005 Plan to (i) increase the authorized shares to 40,000,000 as discussed above and (ii) allow certain unilateral amendments to outstanding options and RSU grants. Shareholder approval for such amendments was not required under Cayman law and we used the home-country exemption for foreign private issuers under Nasdaq rules to effect such amendments without a shareholder vote. In 2009, the Company cancelled 1,221,875 RSUs. There were no changes to outstanding options in 2009. In 2010, the Company exchanged 4,369 thousand stock options for 3,785 thousand new stock options with a similar value.

*Future amendments and termination.* The board of directors may amend (subject to shareholder approval as required by applicable law), suspend or terminate the 2015 Plan at any time. The 2015 Incentive Plan will terminate pursuant to its terms on June 3, 2025.

### ***Employees***

The following table sets forth the number of our employees categorized by function as of the dates indicated.

	<b>As of December 31,</b>		
	<b>2015</b>	<b>2016</b>	<b>2017</b>
Management and administration . . . . .	117	121	128
Operations . . . . .	37	41	42
Research and development . . . . .	640	767	861
Sales and marketing . . . . .	179	193	219
Total . . . . .	<u>973</u>	<u>1,122</u>	<u>1,250</u>

As of December 31, 2017, we had 1,250 total employees, including 800 in Taiwan, 34 in the United States, 255 in China, 154 in Korea, and 7 in Japan. 1,012 of our total employees are engineers.

We do not have any collective bargaining arrangements with our employees and consider our relations with our employees to be good.

### ***Share Ownership***

Under U.S. securities law, a person is deemed to be a “beneficial owner” of a security if that person has or shares “voting power,” which includes the power to vote or to direct the voting of such security, or “investment power,” which includes the power to dispose of or to direct the disposition of such security. A person is also deemed to be the beneficial owner of any securities of which that person has a right to acquire beneficial ownership within 60 days. Under these rules, more than one person may be deemed a beneficial owner of securities as to which such person has no economic interest.

There were 144,423,180 of our ordinary shares outstanding as of March 31, 2018. The following table sets forth information with respect to the beneficial ownership of our ordinary shares as of March 31, 2018, less otherwise indicated in the footnotes, by each of our directors and officers:

	Shares Beneficially Owned	
	Number	%
<b>Executive Officers and Directors:</b>		
James Chow <sup>(1)</sup> . . . . .	2,341,266	1.62
Wallace C. Kou <sup>(2)</sup> . . . . .	3,295,594	2.28
Steve Chen <sup>(3)</sup> . . . . .	30,000	*
Tsung-Ming Chung <sup>(4)</sup> . . . . .	60,000	*
Lien-Chun Liu <sup>(5)</sup> . . . . .	214,280	*
Yung-Chien Wang <sup>(6)</sup> . . . . .	818,674	*
Han-Ping D. Shieh <sup>(7)</sup> . . . . .	38,800	*
Riyadh Lai <sup>(8)</sup> . . . . .	1,772,380	1.23
Nelson Duann <sup>(9)</sup> . . . . .	36,000	*
Sangwoo Han <sup>(10)</sup> . . . . .	106,608	*
Xueshi Yang <sup>(11)</sup> . . . . .	790,188	*
Arthur Yeh <sup>(12)</sup> . . . . .	155,248	*
Robert Fan <sup>(13)</sup> . . . . .	62,000	*
John (Chun-O) Kim <sup>(14)</sup> . . . . .	43,600	*
David Yu <sup>(15)</sup> . . . . .	11,248	*
Frank Chang <sup>(16)</sup> . . . . .	19,440	*
Ken Chen <sup>(17)</sup> . . . . .	196,049	*
Kevin Yeh <sup>(18)</sup> . . . . .	71,600	*
John (Jong Ryul) Lee <sup>(19)</sup> . . . . .	27,504	*
Derek Zhou <sup>(20)</sup> . . . . .	472,476	*
Leander Yu . . . . .	—	*
Jason Chiang <sup>(21)</sup> . . . . .	451,263	*
Frank Shu <sup>(22)</sup> . . . . .	51,000	*
Mike Jing <sup>(23)</sup> . . . . .	7,500	*

\* Less than one percent

- (1) Represents 2,341,266 shares owned by Mr. Chow. Mr. Chow is the chairman of Concord Consulting Inc. and Concord Financial Co. Ltd. which owned 42,445 and 196,491 shares, respectively. Mr. Chow disclaims any beneficial ownership of these shares.
- (2) Represents 2,860,500 shares owned by Mr. Kou, 435,094 shares owned by his family members.
- (3) Represents 30,000 shares owned by Mr. Chen.
- (4) Represents 60,000 shares owned by Mr. Chung.
- (5) Represents 214,280 shares owned by Ms. Liu.
- (6) Represents 818,674 shares owned by Mr. Wang.
- (7) Represents 38,800 shares owned by Mr. Shieh.
- (8) Represents 952,500 shares owned by Mr. Lai and 819,880 shares owned by his spouse.
- (9) Represents 36,000 shares owned by Mr. Duann.
- (10) Represents 106,608 shares owned by Mr. Han.
- (11) Represents 16,000 shares owned by Mr. Yang and 774,188 shares owned by Mr. Yang's holding company.
- (12) Represents 155,248 shares owned by Mr. Yeh.
- (13) Represents 62,000 shares owned by Mr. Fan.
- (14) Represents 43,600 shares owned by Mr. Kim.
- (15) Represents 11,248 shares owned by Mr. Yu.
- (16) Represents 19,440 shares owned by Mr. Chang.

- (17) Represents 190,324 shares owned by Mr. Chen and 5,725 shares owned by his spouse.
- (18) Represents 71,600 shares owned by Mr. Yeh.
- (19) Represents 27,504 shares owned by Mr. Lee.
- (20) Represents 15,000 shares owned by Mr. Zhou and 457,476 shares owned by Mr. Zhou's holding company.
- (21) Represents 439,813 shares owned by Mr. Chiang and 11,450 shares owned by his spouse.
- (22) Represents 51,000 shares owned by Mr. Shu.
- (23) Represents 7,500 shares owned by Mr. Jing.

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

**Major Shareholders**

As of March 31, 2018, there were 144,423,180 of our ordinary shares outstanding. The Bank of New York Mellon, the depository under our ADS deposit agreement, has advised us that as of March 31, 2018, we had 36,028,129 ADSs, representing 144,112,516 ordinary shares.

The following table sets forth information with respect to the beneficial ownership of more than 5% of our ordinary shares as of March 31, 2018:

<u>Identity of person or group</u>	<u>Number of shares owned</u>	<u>Percentage Owned <sup>(1)</sup></u>
Lazard Asset Management LLC . . . . .	9,116,780 <sup>(2)</sup>	6.3%
ARGA Investment Management, LP and Avula Rama Krishna. . . . .	8,355,084 <sup>(3)</sup>	5.8%

- (1) Based on 144,423,180 ordinary shares outstanding as of March 31, 2018.
- (2) Lazard Asset Management LLC held 2,279,195 ADSs (representing 9,116,780 ordinary shares), according to a Schedule 13G dated February 9, 2018.
- (3) ARGA Investment Management, LP and Avula Rama Krishna held 2,088,771 ADSs (representing 8,355,084 ordinary shares), according to a Schedule 13G dated February 9, 2018.

To our knowledge, we are not owned or controlled, directly or indirectly, by another corporation, by any foreign government or by any other natural or legal persons, severally or jointly. We are not aware of any arrangement which may at a later date result in a change of control of our company.

No holder of our ordinary shares has preferential voting rights.

**Related Party Transactions**

No related party transactions occurred between January 1, 2015 and April 26, 2018 (other than ordinary course compensation paid to employees, officers and directors and described elsewhere in this annual report).

**ITEM 8. FINANCIAL INFORMATION**

**Consolidated Financial Statements**

See "Item 18. Financial Statements" and pages F-1 through F-40 of this annual report.

**Legal Proceedings**

As an active operating company, we are subject to legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. Although the outcome of such proceedings and claims cannot be predicted with certainty, management does not believe that the outcome of any of these matters will have a material adverse effect on our business, results of operations, financial position or cash flows. Any litigation, however, involves potential risk and potentially significant litigation costs, and therefore there can be no assurance that any litigation which is now pending or which may arise in the future would not have such material adverse effect on our business, financial position, results of operations or cash flows.



All American Semiconductor, Inc. (“All American” or “AASI”) was a former distributor for the Company. On April 25, 2007, All American filed for Chapter 11 bankruptcy protection. At the time of the filing, the Company had US\$256 thousand of unpaid accounts receivable from All American. On April 17, 2009 SMI USA and related entities were named as defendants in an adversary proceeding filed by the AASI Creditor Liquidating Trust (“CLT”) in the bankruptcy case pending in the U.S. Bankruptcy Court for the Southern District of Florida. The CLT was seeking the return of allegedly avoidable transfers in the amount of US\$854 thousand. SMI USA filed an answer and affirmative defenses. In March 2010, SMI USA settled with the CLT by paying the amount of US\$220 thousand and on April 1, 2010, the Bankruptcy Court granted the motion to approve stipulations to compromise controversy. On August 23, 2010, the Court entered an order dismissing the adversary proceeding. In June 2011, Liquidating Trustee for the CLT filed the AASI Creditor Liquidating Trustee’s Seventeenth Omnibus Objection to Claims but in August 2011, withdrew it with respect to SMI USA’s proof of claim. As a holder of allowed claims, we are entitled to receive distribution pursuant to the bankruptcy plan. On December 31, 2017, we received total distributions of US\$265 thousand from the CLT. We are not expecting further distributions.

In 2006, FCI joined with other technology companies and invested in the Pangyo Silicon Park Construction Project Cooperative (“Pangyo Cooperative”) in Korea. In July 2010, FCI, TLI Inc. (“TLI”), OCI Materials Co., Ltd (“OCI”) and other companies withdrew from the Pangyo Cooperative and forfeited 10% of their total investment. FCI believes its loss was caused by bad will actions taken by TLI. In December 2011, FCI and OCI together filed a complaint against TLI at the Suwon District Court in Korea. In April 2013, the court dismissed the plaintiffs’ complaints. The plaintiffs have decided not to appeal the court’s decision. This case is officially closed.

#### **Policy on Dividend Distributions**

Pursuant to the laws and regulations of the ROC and the Articles of Incorporation of SMI Taiwan, our subsidiary in Taiwan must make appropriations from annual earnings to a non-distributable reserve which could affect our ability to pay cash or stock dividends, if any. The Taiwan subsidiary may only distribute dividends after it has made allowances as determined under ROC GAAP at each year-end for:

- a. Payment of taxes;
- b. Recovery of prior years’ deficits, if any;
- c. 10% of remaining balance after deduction for a and b as legal reserve;
- d. Special reserve based on relevant laws or regulations or 10% of remaining balance for deduction from above a to c as special reserve when necessary.

#### **Dividends**

We paid a total of \$22.9 million and \$32.1 million in dividends during 2016 and 2017, respectively. On October 24, 2016 and October 24, 2017, our Board of Directors, instead of declaring a quarterly dividend, declared an annual dividend payable in four quarterly installments. Future dividends, if any, on our outstanding ADSs and ordinary shares will be declared by and subject to the discretion of our board of directors. If our board of directors decides to distribute dividends, the form, frequency and amount of such dividends will depend upon our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors our board of directors may deem relevant. Any future dividend we declare will be paid to the holders of ADSs, subject to the terms of the deposit agreement, to the same extent as holders of our ordinary shares, to the extent permitted by applicable laws and regulations, less the fees and expenses payable under the deposit agreement. Any dividend we declare will be distributed by the depository bank to the holders of our ADSs. Cash dividends on our ordinary shares, if any, will be paid in U.S. dollars.

#### **Significant Changes**

No significant changes have occurred since the date of our audited consolidated financial statements.

## ITEM 9. THE OFFER AND LISTING

### Market and Share Price Information

Our ADSs, each representing four of our ordinary shares, have been listed on Nasdaq since June 30, 2005. Our ADSs trade under the symbol “SIMO.” The Nasdaq Global Select Market is the principal trading market for our ADSs, which are not listed on any other exchanges in or outside the United States. The high and low sales prices of our ADSs on Nasdaq since 2013 are as follows:

	Price per ADS (US\$)	
	High	Low
<b>Annual:</b>		
2013 .....	16.19	9.90
2014 .....	28.96	12.92
2015 .....	37.60	20.01
2016 .....	55.85	27.41
2017 .....	55.68	37.37
<b>Quarterly:</b>		
First Quarter, 2016 .....	39.89	27.41
Second Quarter, 2016 .....	47.80	36.90
Third Quarter, 2016 .....	55.85	47.74
Fourth Quarter, 2016 .....	53.17	40.43
First Quarter, 2017 .....	47.33	37.37
Second Quarter, 2017 .....	55.68	44.00
Third Quarter, 2017 .....	49.85	40.33
Fourth Quarter, 2017 .....	55.12	46.50
First Quarter 2018 .....	56.51	42.57
<b>Monthly</b>		
November 2017 .....	52.84	46.51
December 2017 .....	55.12	50.74
January 2018 .....	56.51	45.51
February 2018 .....	50.88	42.57
March 2018 .....	50.19	44.74
April 2018 <sup>(1)</sup> .....	49.68	46.00

(1) Through April 27, 2018.

## ITEM 10. ADDITIONAL INFORMATION

### Memorandum and Articles of Association

The information called for by Item 10B (“Memorandum and Articles of Association”) is incorporated by reference to the information under the heading “Description of Share Capital” in our Registration Statement on Form F-1, as amended (Registration Number 333-125673) and as filed with the SEC on June 5, 2005.

### Material Contracts

We have not entered into any material contracts within the past two fiscal years other than in the ordinary course of business and other than those described in Item 4, “Information on the Company” or elsewhere in this annual report.

### Exchange Controls

See “Policy on Dividend Distributions” above.

## **Taxation**

### **United States Federal Income Taxation**

The following discussion summarizes certain U.S. federal income tax consequences to a U.S. Holder, as defined below, who purchases our ADSs and ordinary shares. This discussion assumes that investors will hold their ADSs or ordinary shares as capital assets (generally, property held for investment). This discussion does not discuss all aspects of U.S. federal income taxation which may be important to particular investors in light of their individual circumstances, including investors subject to special taxation, such as:

- banks and financial institutions;
- brokers and dealers in securities or currencies;
- insurance companies;
- tax-exempt organizations and retirement plans;
- grantor trusts;
- S corporations;
- persons holding ADSs or ordinary shares as part of hedging, conversion, constructive sale, straddle or other integrated transactions;
- persons who acquired their ordinary shares upon the exercise of employee stock options or otherwise as compensation;
- persons who have elected the mark-to-market method of accounting;
- persons who own 10% or more of our ADSs or shares;
- real estate investment trusts or regulated investment companies;
- U.S. persons whose “functional currency” is not the U.S. dollar;
- certain former citizens or long-term residents of the United States; and
- Non-U.S. Holders (as defined below).

This discussion is based in part on representations by the depositary and assumes that each obligation under the deposit agreement and any related agreement will be performed in accordance with its terms. Furthermore, the discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended (the “Code”), and U.S. Treasury regulations, rulings and judicial decisions hereunder as of the date hereof. Such authorities are subject to change, possibly on a retroactive basis, which may result in U.S. federal income tax consequences different from those discussed below.

**A person considering an investment in our ADSs or ordinary shares is urged to consult its tax advisor concerning U.S. federal, state, local and non-U.S. income and other tax consequences.**

A U.S. Holder is a beneficial owner of ADSs or ordinary shares that is for U.S. federal income tax purposes:

- a citizen or resident individual of the United States;
- a corporation or other entity taxable as a corporation created or organized in or under the laws of the United States, any state thereof, or the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation, regardless of its source; or
- a trust if it 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 substantial decisions of the trust or has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.

A beneficial owner of ADSs or ordinary shares that is not a U.S. Holder is referred to herein as a “Non-U.S. Holder.” If a partnership or limited liability company treated as a partnership for U.S. federal income tax purposes holds ADSs or ordinary shares, the tax treatment of a partner or member will generally depend on the status of the partner or member and the activities of the partnership or such limited liability company. A partner of a partnership or a member of such a limited liability company holding ADSs or ordinary shares is urged to consult its tax advisors regarding an investment in our ADSs or ordinary shares.

*ADSs.* In general, for U.S. federal income tax purposes, a U.S. Holder of ADSs will be treated as the owner of the underlying ordinary shares that are represented by such ADSs. Deposits and withdrawals of ordinary shares in exchange for ADSs will not be subject to U.S. federal income taxation.

*Distributions on ADSs or ordinary shares.* Unless the passive foreign investment company rules, as discussed below, apply, the gross amount of the distributions in respect of the ADSs or ordinary shares will be subject to tax as dividend income to the extent of our current and accumulated earnings and profits, as determined under U.S. federal income tax principles. Subject to certain limitations, dividends paid to non-corporate U.S. Holders, including individuals, may be eligible for a reduced rate of taxation if we are deemed to be a “qualified foreign corporation” for U.S. federal income tax purposes, provided that such holder satisfies certain holding period requirements with respect to the ownership of our ADSs or ordinary shares. Subject to the exceptions discussed below, a corporation is a qualified foreign corporation if it is:

- a foreign corporation that is eligible for the benefits of a comprehensive income tax treaty with the United States that includes an exchange of information program; or
- a foreign corporation if its stock with respect to which a dividend is paid or its ADSs backed by such stock are readily tradable on an established securities market within the United States.

The Cayman Islands does not currently have a comprehensive income tax treaty with the United States. A foreign corporation (even if it is described above) does not constitute a qualified foreign corporation if, for the taxable year in which the dividend is paid or the preceding taxable year, the foreign corporation is or was a passive foreign investment company. Although we believe that we are a qualified foreign corporation because the ADSs will be traded on an established U.S. securities market and, as discussed below, we believe that we were not a passive foreign investment company for our 2017 tax year, no assurance can be given in this regard. In addition, our status as a qualified foreign corporation may change. A U.S. Holder that exchanges its ADSs for ordinary shares may not be eligible for the reduced rate of taxation on dividends if the ordinary shares are not deemed to be readily tradable on an established securities market within the United States.

Dividends will be includable in a U.S. Holder’s gross income on the date actually or constructively received by the depository, in the case of ADSs or, in the case of ordinary shares, by such U.S. Holder. These dividends will not be eligible for the dividends-received deduction generally allowed to U.S. corporations in respect of dividends received from other U.S. corporations.

To the extent we pay dividends on the ADSs or ordinary shares in a currency other than the U.S. dollar, the U.S. dollar value of such dividends should be calculated by reference to the exchange rate prevailing on the date of actual or constructive receipt of the dividend, regardless of whether the foreign currency is converted into U.S. dollars at that time. If the foreign currency is converted into U.S. dollars on the date of actual or constructive receipt of such dividends, the tax basis of the U.S. Holder in such foreign currency will be equal to its U.S. dollar value on that date and, as a result, the U.S. Holder generally should not be required to recognize any foreign currency exchange gain or loss. Dividends paid in respect of the ADSs or ordinary shares generally will be treated as income from sources outside the United States.

To the extent that the amount of any distribution exceeds our current and accumulated earnings and profits, the distribution will first be treated as a tax-free return of capital, causing a reduction in the adjusted basis of the ADSs or ordinary shares, and the balance in excess of adjusted basis will be taxed as capital gain.

*Sale, exchange or other disposition of ADSs or ordinary shares.* Unless the passive foreign investment company rules, as discussed below, apply, upon the sale, exchange or other disposition of ADSs or ordinary shares a U.S. Holder generally will recognize capital gain or loss equal to the difference between the amount realized upon the sale, exchange or other disposition and the adjusted tax basis of the U.S. Holder in the ADSs or ordinary shares. The capital gain or loss generally will be long-term capital gain or loss if, at the time of sale, exchange or other disposition, the U.S. Holder has held the ADS or ordinary share for more than one year. Net long-term capital gains of non-corporate U.S. Holders, including individuals, are eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations. Any gain or loss that a U.S. Holder recognizes generally will be treated as gain or loss from sources within the United States for U.S. foreign tax credit limitation purposes.

*Additional tax on net investment income.* An additional 3.8% federal income tax may be assessed on net investment income (including dividends, other distributions, and gain realized on the sale of ADSs or ordinary shares) earned by certain U.S. Holders. This tax does not apply to U.S. Holders who hold ADSs or ordinary shares in the ordinary course of certain trades or businesses.

*Passive foreign investment company rules.* In general, we will be classified as a passive foreign investment company for any taxable year in which either (a) at least 75% of our gross income is passive income or (b) at least 50% of the value (determined on the basis of a quarterly average) of our assets is attributable to assets that produce or are held for the production of passive income. For this purpose, passive income generally includes dividends, interest, royalties, rents (other than rents and royalties derived in the active conduct of a trade or business and not derived from a related person), annuities and gains from assets that produce passive income. If we own directly or indirectly at least 25% by value of the equity shares of another corporation, we will be treated for purposes of the passive foreign investment company tests as owning a proportionate share of the assets of the other corporation, and as receiving directly a proportionate share of the other corporation's income.

We believe, based on our present and projected composition of our income and valuation of our assets, we were not classified as a passive foreign investment company for U.S. federal income tax purposes for our 2017 tax year, although no assurance can be given in this regard. Whether we are a passive foreign investment company for any particular taxable year is determined on an annual basis and will depend on the composition of our income and assets, including goodwill. The calculation of goodwill will be based, in part, on the then market value of our capital stock, which is subject to fluctuation. Accordingly, there can be no assurance that we will not be classified as a passive foreign investment company in the current or any future taxable year.

If we are a passive foreign investment company for any taxable year during which a U.S. Holder has an equity interest in our company, unless the U.S. Holder makes a mark-to-market election as discussed below, such U.S. Holder will be subject to special tax rules in any future taxable year regardless of whether we are classified as a passive foreign investment company in such future years with respect to (a) "excess distributions" and (b) gain from the disposition of stock. Excess distributions are defined generally as the excess of the amount received with respect to the equity interests in the taxable year over 125% of the average annual distributions received in the shorter of either the three previous years or a U.S. Holder's holding period before the taxable year and must be allocated ratably to each day of the U.S. Holder's holding period. The amount allocated to the current taxable year or any year before we became a passive foreign investment company will be included as ordinary income in a U.S. Holder's gross income for that year. The amount allocated to other prior taxable years will be taxed as ordinary income at the highest rate in effect for a U.S. Holder in that prior year and the tax is subject to an interest charge at the rate applicable to deficiencies in income taxes. The entire amount of any gain realized upon the sale or other disposition of the equity interests will be treated as an excess distribution made in the year of sale or other disposition and as a consequence will be treated as ordinary income and, to the extent allocated to years prior to the year of sale or disposition with respect to which we were a passive foreign investment company, will be subject to the interest charge described above.

In certain circumstances, instead of being subject to the excess distribution rules discussed above, a U.S. Holder may make an election to include gain on the ADSs or ordinary shares of a passive foreign

investment company as ordinary income under a mark-to-market method, provided that the ADSs or ordinary shares are regularly traded on a qualified exchange. Under current law, the mark-to-market election is only available for ADSs or ordinary shares that are regularly traded within the meaning of U.S. Treasury regulations on certain designated U.S. exchanges and foreign exchanges that meet trading, listing, financial disclosure and other requirements to be treated as a qualified exchange under applicable U.S. Treasury regulations. The Nasdaq Stock Market is a qualified exchange. The ordinary shares may not be eligible for mark-to-market treatment under the foregoing rule even if the ADSs otherwise satisfy the applicable requirement.

If a U.S. Holder makes a mark-to-market election, the U.S. Holder will include each year as ordinary income, rather than capital gain, the excess, if any, of the fair market value of the U.S. Holder's ADSs or ordinary shares at the end of the taxable year over such U.S. Holder's adjusted basis in the ADSs (or ordinary shares, if applicable) and will be permitted an ordinary loss in respect of the excess, if any, of the adjusted basis of these ADSs or ordinary shares over their fair market value at the end of the taxable year, but only to the extent of the net amount previously included in income as a result of the mark-to-market election. A U.S. Holder's basis in the ADSs or ordinary shares will be adjusted to reflect any such income or loss amounts. Any gain or loss on the sale of the ADSs or ordinary shares will be ordinary income or loss, except that this loss will be ordinary loss only to the extent of the previously included net mark-to-market gain.

If we are a passive foreign investment company, then under certain circumstances a U.S. Holder must file Internal Revenue Service Form 8621.

*Information Reporting and Back-up Withholding.* The Foreign Account Tax Compliance Act ("FATCA") generally requires that individuals that hold certain specified foreign financial assets worth in excess of certain thresholds of \$50,000 or more, depending on the individual's circumstances, report such ownership to the IRS using IRS Form 8938. The definition of specified foreign financial assets includes not only financial accounts maintained in foreign financial institutions, but also, unless held in accounts maintained by a financial institution, any stock or security issued by a non-U.S. person, any financial instrument or contract held for investment that has an issuer or counterparty other than a U.S. person and any interest in a foreign entity. A U.S. Holder may be subject to this reporting requirement unless such holder's ADSs or ordinary shares are held in an account at a domestic financial institution. The penalty for failing to file Form 8938 is substantial.

U.S. holders generally are subject to information reporting requirements with respect to dividends on, or proceeds from the disposition of, our ordinary shares. In addition, a U.S. holder may be subject, under certain circumstances, to backup withholding at a rate of up to 24% with respect to dividends paid on, or proceeds from the disposition of, our ordinary shares unless the U.S. holder provides proof of an applicable exemption or correct taxpayer identification number, and otherwise complies with the applicable requirements of the backup withholding rules. A U.S. holder of our ordinary shares who provides an incorrect taxpayer identification number may be subject to penalties imposed by the IRS. Amounts withheld under the backup withholding rules are not an additional tax and may be refunded or credited against the U.S. holder's U.S. federal income tax liability, provided the required information is furnished to the IRS.

A U.S. Holder is urged to consult its tax advisor concerning the U.S. federal income tax consequences of an investment in our ADSs or ordinary shares if we are or become a passive foreign investment company, including the possibility of making a mark-to-market election.

### **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 our company 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. The Cayman Islands are not party to any double taxation treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.



We have, pursuant to Section 6 of the Tax Concessions Law (1999 Revision) of the Cayman Islands, obtained an undertaking from the Governor-in-Council that:

- no law which is enacted in the Cayman Islands imposing any tax to be levied on profits or income or gains or appreciation applies to us or our operations; and
- the aforesaid tax or any tax in the nature of estate duty or inheritance tax are not payable on our ordinary shares, debentures or other obligations.

The undertaking that we have obtained is for a period of 20 years from March 1, 2005.

## **Documents on Display**

We have previously filed with the SEC our registration statement on Form F-6 under the Securities Act of 1933, as amended (the “Securities Act”) with respect to our ADSs.

We are subject to the periodic reporting and other informational requirements of the U.S. Securities Exchange Act of 1934, as amended (the “Exchange Act”). Under the Exchange Act, we are required to file reports and other information with the SEC. Specifically, we are required to file annually a Form 20-F no later than four months after the close of each fiscal year, which is December 31. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and our officers, directors, and principal shareholders are exempt from the reporting and short-swing profit recovery provisions of Section 16 of the Exchange Act.

Copies of reports and other information, when so filed, may be inspected without charge and may be obtained at prescribed rates at the public reference facilities maintained by the Securities and Exchange Commission at the SEC’s public reference room in Washington D.C. at 100 F Street, N.E., Room 1580, Washington D.C. 20549. You can request copies of these documents upon payment of a duplicating fee, by writing to the SEC. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference rooms. The SEC also maintains a Website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system.

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

*Interest rate risk.* Our exposure to changes in interest rates is limited to interest income generated by our cash deposited with banks and short-term investments maintained in bond funds, principal protected notes and interest expenses payable on our bank loans. We have not entered into any interest rate swap transactions. We do not believe that a 1% change in interest rates would have a significant impact on our operations.

*Foreign currency risk.* Since 2012, we consider our direct exposure to foreign exchange rate fluctuations to be minimal. Prior to 2012, we reported our financial results in NT dollars and our direct exposure to foreign exchange rate fluctuations was more significant. Gains or losses from foreign currency re-measurement are included in “Non-Operating Income (Expenses)” in our Consolidated Financial Statements. The impact of foreign currency transaction gain or loss included in determining net income (loss) for 2015, 2016 and 2017 was US\$0.1 million, US\$(0.7) million and US\$(0.2) million, respectively. Currently, the majority of our revenue, cost of sales, accounts receivable, and accounts payable are denominated in U.S. dollars. Increases in the value of the U.S. dollar relative to other currencies would make our products more expensive, which could negatively impact our ability to compete. Conversely, decreases in the value of the U.S. dollar relative to other currencies could result in our suppliers raising their prices in order to continue doing business with us. Fluctuations in currency exchange rates could harm our business in the future. We do not utilize foreign exchange derivatives contracts to protect against changes in foreign exchange rates.

Also refer to “Risk Factors — We are subject to risks associated with international operations which may harm our business.”

*Investment Risk.* Prior to March 2007, we invested in equity instruments of privately held companies. We have minority stake equity investments in Cashido and Vastview Technology, private companies related to semiconductor and other technology industries. These investments are accounted for under the cost method because our ownership is less than 20% and we do not have the ability to exercise significant influence over the operations of these companies. As of December 31, 2017, the aggregate carrying value of these investments on our balance sheet was nil. We monitor these investments for impairment and make appropriate reductions in carrying value when an impairment is deemed to be other than temporary. The impairments loss for the years ended on December 31, 2015, 2016 and 2017 was nil, US\$13 thousand and US\$120 thousand, respectively.

As of December 31, 2017, we also had the short-term investments of US\$6.1 million in principal protected notes and of US\$0.8 million in bond funds.

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

*Depository Fees and Charges.* For the year-ended December 31, 2017, we received from our depository bank a reimbursement of US\$0.6 million, net of withholding tax, for our continuing annual stock exchange listing fees and our other expenses incurred in connection with maintaining and promoting our ADS program. In addition, the depository bank has agreed to reimburse us annually for a fixed number of years for our continuing annual stock exchange listing fees and our other expenses incurred in connection with maintaining and promoting our ADS program. The amount of annual reimbursements is subject to certain limits.

## PART II

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

Not applicable.

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

Not applicable.

### ITEM 15. CONTROLS AND PROCEDURES

#### Disclosure Controls and Procedures

We performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2017. Disclosure controls and procedures are designed to ensure that the material financial and non-financial information required to be disclosed in this annual report on Form 20-F and filed with the SEC is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. The evaluation was performed with the participation of our key corporate senior management, and under the supervision of our Chief Financial Officer, or CFO, Riyadh Lai, and our President and Chief Executive Officer, or CEO, Wallace Kou. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable, rather than absolute, assurances of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the foregoing, our management, including our CEO and CFO, concluded that our disclosure controls and procedures were effective.

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

Our management, including our CEO and CFO, is responsible for establishing and maintaining adequate internal control over financial reporting, as defined under Exchange Act Rules 13a-15(f) and 15d-15(f). Our 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. 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 our assets, (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 our receipts and expenditures are being made only in accordance with appropriate authorizations; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Our management assessed the effectiveness of our internal control over financial reporting as of the end of the period covered by this annual report based on the criteria set forth in the Internal Control-Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Their assessment included an evaluation of the design of our internal control over financial reporting and testing of the operational effectiveness of our internal control over financial reporting. Based on that assessment, our management concluded that as of December 31, 2017 the company's internal control over financial reporting was effective.

Deloitte & Touche, the independent registered public accounting firm that audited our consolidated financial statements included in this annual report has issued an attestation report regarding internal control over financial reporting.

Our evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2017 excluded the internal control over financial reporting of Bigtera, because Bigtera was acquired on July 3, 2017 and whose financial statements constitute 0.44% and 0.55% of net and total assets, respectively, 0.56% of net sales, and 0.52% of net income of the consolidated financial statement amounts as of and for the year ended December 31, 2017.

#### ***Changes in Internal Control over Financial Reporting***

During 2017, no change to our internal control over financial reporting occurred that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

#### ***Inherent Limitations on Effectiveness of Controls***

All internal control systems no matter how well designed and implemented have inherent limitations. Even systems determined to be effective may not prevent or detect misstatements or fraud and can only provide reasonable assurance with respect to disclosure and financial statement presentation and reporting. Additionally, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changed conditions and the degree of compliance with the policies or procedures may deteriorate.

#### ***Attestation Report Of The Independent Registered Public Accounting Firm***

#### **REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Shareholders and Board of Directors of  
Silicon Motion Technology Corporation

#### ***Opinion on Internal Control over Financial Reporting***

We have audited the internal control over financial reporting of Silicon Motion Technology Corporation and subsidiaries (the “Company”) as of December 31, 2017, based on criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control — Integrated Framework (2013) issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements as of and for the year ended December 31, 2017, of the Company and our report dated April 30, 2018 expressed an unqualified opinion on those financial statements.

As described in Management’s Report on Internal Control over Financial Reporting, management excluded from its assessment the internal control over financial reporting at Bigtera, which was acquired on July 3, 2017 and whose financial statements constitute 0.44% and 0.55% of net and total assets, respectively, 0.56% of net sales, and 0.52% of net income of the consolidated financial statement amounts as of and for the year ended December 31, 2017. Accordingly, our audit did not include the internal control over financial reporting at Bigtera.

#### ***Basis for Opinion***

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 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 are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. 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.

***Definition and Limitations of Internal Control over Financial Reporting***

A company's 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 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 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.

/s/ Deloitte & Touche  
Taipei, Taiwan  
The Republic of China  
April 30, 2018

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

Our board of directors has determined that Mr. Tsung-Ming Chung, the Chairman of our audit committee and an independent director, is an "audit committee financial expert" under Nasdaq and SEC rules.

**ITEM 16B. CODE OF ETHICS**

Our board of directors has adopted a code of business conduct and ethics applicable to every employee of our company, including our CEO and our CFO, consistent with the requirements of the Nasdaq Stock Market. A copy of our code of ethics has been filed with the SEC as Exhibit 11.1 to our annual report on Form 20-F filed on June 30, 2006. For further information, see our Code of Ethics posted on our website ([www.siliconmotion.com](http://www.siliconmotion.com)).

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

Deloitte & Touche has acted as the independent registered public accountants of our company and its subsidiaries for 2016 and 2017. The following table sets forth the aggregate fees by categories specified below in connection with certain professional services rendered by Deloitte & Touche for the periods indicated.

	<u>2016</u>	<u>2017</u>
	US\$	US\$
	(in thousands)	
Audit Fees <sup>(1)</sup> .....	870	880
Audit-Related Fees <sup>(2)</sup> .....	—	—
Tax Fees <sup>(3)</sup> .....	190	213
All Other Fees <sup>(4)</sup> .....	—	—
Total .....	1,060	1,093

- (1) *Audit Fees.* This category includes the audit and review of our annual financial statements and services that are normally provided by the independent auditors in connection with regulatory filings or engagements, consultations provided on audit and accounting matters that arise during, or as a result of, the audits or the reviews of interim financial statements, audit procedures related to reviews of offering documents, registration statements and issuance of comfort letters.
- (2) *Audit-Related Fees.* This category consists of assurance and related services by Deloitte & Touche that are reasonably related to the performance of the audit or review of our financial statements and are not reported above under “Audit Fees.” Deloitte & Touche did not provide any services under this category in 2016 or 2017.
- (3) *Tax Fees.* This category consists of professional services rendered by Deloitte & Touche for tax compliance and tax advice. The services for the fees disclosed in this category include tax return preparation and technical tax advice.
- (4) *All other fees.* Deloitte & Touche did not provide any services under this category in 2016 or 2017.

Our audit committee is responsible for the retention of our independent registered public accounting firm, which currently is Deloitte & Touche. Our audit committee has adopted its own rules of procedure, in the form of an audit committee charter. The audit committee’s rules of procedure provide for a process with respect to the prior approval of all non-audit services to be performed by our independent auditors. Our audit committee reports to our board of directors regarding the scope and results of our annual audits, compliance with our accounting and financial policies and management’s procedures and policies related to the adequacy of our internal accounting controls.

In 2017 our audit committee approved all of the audit services provided by Deloitte & Touche and the other services provided by Deloitte & Touche.

**ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not applicable.

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

Not applicable.

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

Not applicable.



**ITEM 16G. CORPORATE GOVERNANCE**

We are incorporated in the Cayman Islands and our corporate governance practices are governed by applicable Cayman Islands law. In addition, because our ADSs are listed on the Nasdaq Global Select Market, we are subject to Nasdaq corporate governance requirements. Nasdaq Listing Rule 5615(a)(3) permits foreign private issuers like us to follow “home country practice” with respect to certain corporate governance matters, such as, for example, our establishment in 2015 of our 2015 Incentive Plan. We are committed to a high standard of corporate governance. As such, we endeavor to comply with the Nasdaq corporate governance practices and believe that we are currently in compliance with Nasdaq corporate governance practices that are applicable to foreign private issuers.

### PART III

#### ITEM 17. FINANCIAL STATEMENTS

Not applicable.

#### ITEM 18. FINANCIAL STATEMENTS

Our consolidated financial statements are included in this annual report at pages F-1 through F-40.

#### ITEM 19. EXHIBITS

<u>Exhibit Number</u>	<u>Description</u>
1.1	Memorandum of Association of the Registrant (incorporated by reference to Exhibit 3.1 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
1.2	Articles of Association of the Registrant (incorporated by reference to Exhibit 3.2 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
2.1	Specimen of American Depositary Receipt (incorporated by reference to Exhibit 4.1 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
2.2	Form of Deposit Agreement (incorporated by reference to Exhibit 4.2 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
2.3	Second Amended and Restated Silicon Motion Technology Corporation Equity Incentive Plan 2005 (incorporated by reference to Exhibit 2.3 of the company's Form 20-F for the year ended December 31, 2009, filed June 25, 2010).
2.4	Silicon Motion Technology Corporation 2015 Incentive Plan (incorporated by reference to Exhibit 4.1 of the Company's registration statement on Form S-8 filed June 11, 2015).
4.1	Lease Agreement between Silicon Motion, Inc. (Taiwan) and Fang Shinn Industrial Co., Ltd. dated May 4, 2004 (incorporated by reference to Exhibit 10.1 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.2	Lease Agreement between Silicon Motion, Inc. (Taiwan) and TaiHsing Printing and Binding Co., Ltd dated February 23, 2005 (incorporated by reference to Exhibit 10.2 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.3	Lease Agreement between Silicon Motion, Inc. (Taiwan) and Winsome Development Inc. dated November 27, 2003 (incorporated by reference to Exhibit 10.3 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.4	Lease Agreement between Silicon Motion, Inc. (Taiwan) and Richtek Technology Corp. dated February 4, 2005 (incorporated by reference to Exhibit 10.4 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.5	Lease Agreement between Silicon Motion, Inc. (California) and Orchard Investment Company Number 205 dated January 21, 2004 (incorporated by reference to Exhibit 10.5 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).

Exhibit Number	Description
4.6	Bank Line of Credit Agreement between Silicon Motion, Inc. (Taiwan) and Chinatrust Commercial Bank Co., Ltd. dated November 25, 2004 (incorporated by reference to Exhibit 10.6 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.7	Financial Transaction Agreement between Silicon Motion, Inc. (Taiwan) and Chinatrust Commercial Bank Co., Ltd. dated November 25, 2004 (incorporated by reference to Exhibit 10.7 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.8	Specific Clause Agreement between Silicon Motion, Inc. (Taiwan) and Chinatrust Commercial Bank Co., Ltd. dated November 25, 2004 (incorporated by reference to Exhibit 10.8 to the company's Registration Statement on Form F-1 (file no. 333-125673) filed with the Securities and Exchange Commission on June 9, 2005).
4.11	Purchase and Supply Agreement between Lexar Media, Inc. and Silicon Motion Technology Corporation, dated September 1, 2005 (incorporated by reference to Exhibit 4.11 to the Company's Annual Report on Form 20-F filed with the Securities and Exchange Commission on June 30, 2006).
4.12	Share Purchase Agreement dated as of April 18, 2007 among Silicon Motion Technology Corporation, Lake Tahoe Investment Corporation, FCI Inc. and Kwang Jun Yun and the shareholders of FCI (incorporated by reference to Exhibit 4.12 to the Company's Annual Report on Form 20-F filed with the Securities and Exchange Commission on July 2, 2007).
4.13	Share Purchase Agreement dated as of April 24, 2015 among Silicon Motion Technology Corporation, Silicon Motion Technology (Hong Kong) Ltd., F-Tec Holdings International Ltd., the shareholders of F-Tec Holdings International Ltd. and Xueshi Yang, as the Sellers' Representative (incorporated by reference to Exhibit 4.13 to the Company's Annual Report on Form 20-F filed with the Securities and Exchange Commission on April 30, 2015).
8.1 *	List of Subsidiaries.
11.1	Code of Ethics (incorporated by reference to Exhibit 11.1 to the company's Annual Report on Form 20-F filed with the Securities and Exchange Commission on June 30, 2006).
12.1 *	Certification of Chief Executive Officer Required by Rule 13a-14(a).
12.2 *	Certification of Chief Financial Officer Required by Rule 13a-14(a).
13.1 *	Certification of Chief Executive Officer and Chief Financial Officer required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
23.1 *	Consent of Deloitte & Touche.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed herewith.

**SIGNATURES**

The registrant hereby certifies that it meets all 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.

**SILICON MOTION TECHNOLOGY CORPORATION**

**By:** \_\_\_\_\_ /s/ WALLACE C. KOU  
**Wallace C. Kou,**  
**President and Chief Executive Officer**

Date: April 30, 2018

**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**  
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## **REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Shareholders and Board of Directors of  
Silicon Motion Technology Corporation

### **Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Silicon Motion Technology Corporation and subsidiaries (the “Company”) as of December 31, 2016 and 2017, the related consolidated statements of income, comprehensive income, changes in shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2016 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, 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) (PCAOB), the Company’s internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 30, 2018, expressed an unqualified opinion on the Company’s internal control over financial reporting.

### **Basis for Opinion**

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Deloitte & Touche  
Taipei, Taiwan  
The Republic of China  
April 30, 2018

We have served as the Company’s auditor since 1999.



**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

(In Thousands, Except Par Value)

	December 31	
	2016	2017
	US\$	US\$
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents . . . . .	274,483	359,453
Short-term investments . . . . .	3,302	6,941
Notes and accounts receivable, net . . . . .	73,599	79,135
Inventories . . . . .	71,887	94,186
Restricted assets-current . . . . .	44,393	19,515
Noncurrent assets held for sale . . . . .	3,363	—
Prepaid expenses and other current assets . . . . .	5,873	9,567
Total current assets . . . . .	476,900	568,797
Long-term investments . . . . .	120	—
Property and equipment, net . . . . .	47,892	51,370
Deferred income tax assets, net . . . . .	3,983	3,402
Goodwill . . . . .	68,656	58,964
Intangible assets, net . . . . .	5,227	7,429
Other assets . . . . .	3,248	3,770
Total assets . . . . .	606,026	693,732
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities		
Notes and accounts payable . . . . .	31,739	56,423
Bank loan . . . . .	25,000	25,000
Income tax payable . . . . .	20,271	11,492
Current portion of long-term payable . . . . .	240	566
Accrued expenses and other current liabilities . . . . .	68,736	83,763
Total current liabilities . . . . .	145,986	177,244
Long-term payable, net of current portion . . . . .	367	108
Other long-term liabilities . . . . .	16,910	22,329
Total liabilities . . . . .	163,263	199,681
Commitments and Contingencies (Note 18)		
Shareholders' Equity		
Ordinary Shares at US\$ 0.01 par value per share		
Authorized: 500,000 thousand shares		
Issued and outstanding: 141,311 thousand shares in 2016 and 143,162 thousand shares in 2017 . . . . .	1,413	1,431
Additional paid-in capital . . . . .	226,658	242,487
Accumulated other comprehensive income (loss) . . . . .	(1,032)	2,643
Retained Earnings . . . . .	215,724	247,490
Total shareholders' equity . . . . .	442,763	494,051
Total liabilities and shareholders' equity . . . . .	606,026	693,732

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

**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF INCOME**

**(In Thousands, Except Earnings Per Share)**

	Year Ended December 31		
	2015	2016	2017
	US\$	US\$	US\$
NET SALES .....	361,297	556,146	523,404
COST OF SALES .....	176,765	281,541	272,210
GROSS PROFIT .....	184,532	274,605	251,194
OPERATING EXPENSES			
Research and development .....	71,161	92,405	102,053
Sales and marketing .....	20,173	25,765	25,868
General and administrative .....	15,714	17,072	16,933
Impairment of goodwill .....	—	—	10,337
Amortization of intangible assets .....	1,051	2,103	2,534
Gain from disposal of noncurrent assets held for sale .....	—	—	(1,880)
Total operating expenses .....	108,099	137,345	155,845
OPERATING INCOME .....	76,433	137,260	95,349
NON-OPERATING INCOME (EXPENSES)			
Gain from disposal of short-term investments .....	3	2	103
Interest income .....	2,025	2,158	4,268
Foreign exchange gain (loss), net .....	76	(692)	(157)
Impairment of long-term investments .....	—	(13)	(120)
Interest expense .....	(47)	(127)	(423)
Other income (loss), net .....	10	42	(19)
Total non-operating income .....	2,067	1,370	3,652
INCOME BEFORE INCOME TAX .....	78,500	138,630	99,001
INCOME TAX EXPENSE .....	18,249	27,690	24,046
NET INCOME .....	60,251	110,940	74,955
EARNINGS PER ORDINARY SHARE:			
Basic .....	0.44	0.79	0.53
Diluted .....	0.43	0.78	0.52
WEIGHTED AVERAGE ORDINARY SHARES OUTSTANDING			
Basic (Thousands) .....	138,100	140,919	142,738
Diluted (Thousands) .....	139,634	142,050	143,606
EARNINGS PER ADS (one ADS equals four ordinary shares):			
Basic .....	1.75	3.15	2.10
Diluted .....	1.73	3.12	2.09
WEIGHTED AVERAGE ADS OUTSTANDING			
Basic (Thousands) .....	34,525	35,230	35,684
Diluted (Thousands) .....	34,909	35,513	35,902

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

**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(In Thousands)

	<u>Year Ended December 31</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
	US\$	US\$	US\$
NET INCOME .....	60,251	110,940	74,955
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX EFFECT OF NIL			
Change in net foreign currency translation adjustments .....	(1,868)	(1,555)	3,390
Change in deferred pension gain (loss) .....	(4)	(110)	285
OTHER COMPREHENSIVE INCOME (LOSS) .....	<u>(1,872)</u>	<u>(1,665)</u>	<u>3,675</u>
TOTAL COMPREHENSIVE INCOME .....	<u>58,379</u>	<u>109,275</u>	<u>78,630</u>

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

**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**  
(In Thousands, Except Per Share Data)

	Ordinary Share		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Shareholders' Equity
	Shares	Amount				
	(thousands)	US\$	US\$	US\$	US\$	US\$
BALANCE, JANUARY 1, 2015	135,622	1,356	190,783	2,505	109,456	304,100
Net income	—	—	—	—	60,251	60,251
Other comprehensive income	—	—	—	(1,872)	—	(1,872)
Issuance of ordinary shares for Shannon Systems acquisition	1,560	16	7,624	—	—	7,640
Stock-based compensation expenses	—	—	10,418	—	—	10,418
Issuance of ordinary shares upon exercise of employee stock options and restricted stock units	2,339	23	418	—	—	441
Dividends declared (US\$0.2625 per ordinary share)	—	—	—	—	(36,480)	(36,480)
BALANCE, DECEMBER 31, 2015	139,521	1,395	209,243	633	133,227	344,498
Net income	—	—	—	—	110,940	110,940
Other comprehensive income	—	—	—	(1,665)	—	(1,665)
Stock-based compensation expenses	—	—	17,364	—	—	17,364
Issuance of ordinary shares upon exercise of employee stock options and restricted stock units	1,790	18	51	—	—	69
Dividends declared (US\$0.20 per ordinary share)	—	—	—	—	(28,443)	(28,443)
BALANCE, DECEMBER 31, 2016	141,311	1,413	226,658	(1,032)	215,724	442,763
Net income	—	—	—	—	74,955	74,955
Other comprehensive income	—	—	—	3,675	—	3,675
Stock-based compensation expenses	—	—	15,494	—	—	15,494
Issuance of ordinary shares upon exercise of employee stock options and restricted stock units	1,851	18	335	—	—	353
Dividends declared (US\$0.30 per ordinary share)	—	—	—	—	(43,189)	(43,189)
BALANCE, DECEMBER 31, 2017	143,162	1,431	242,487	2,643	247,490	494,051

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

**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In Thousands)

	Year Ended December 31		
	2015	2016	2017
	As Adjusted (Note 2) US\$	(Note 2) US\$	(Note 2) US\$
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income	60,251	110,940	74,955
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	7,936	9,482	10,599
Amortization of intangible assets	1,051	2,103	2,534
Gain from disposal of short-term investments	(3)	(2)	(103)
Impairment of long-term investments	—	13	120
Stock-based compensation	10,418	17,364	15,494
Loss on disposal of property and equipment	10	33	4
Impairment of goodwill	—	—	10,337
Gain from disposal of noncurrent assets held for sale	—	—	(1,880)
Deferred income taxes	911	(3,373)	581
Changes in operating assets and liabilities:			
Short-term investments	—	(2,710)	(3,208)
Notes and accounts receivable	(29,179)	(14,620)	(5,156)
Inventories	(410)	(24,777)	(22,299)
Prepaid expenses and other current assets	(664)	(1,313)	1,585
Other assets	136	(5)	(138)
Notes and accounts payable	7,651	9,198	24,248
Accrued expenses and other current liabilities	11,020	12,180	458
Income tax payable	(4,301)	6,876	(8,779)
Other liabilities	1,119	4,179	4,529
Net cash provided by operating activities	<u>65,946</u>	<u>125,568</u>	<u>103,881</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchase of held-to-maturity financial assets	(4,000)	—	—
Proceeds from sale of held-to-maturity financial assets	—	4,000	—
Business acquisition-net of cash, cash equivalents, and restricted cash acquired	(30,286)	—	(2,865)
Increase of prepaid expenses and other current assets	(508)	—	—
Purchase of property and equipment	(23,664)	(12,220)	(11,683)
Net cash used in investing activities	<u>(58,458)</u>	<u>(8,220)</u>	<u>(14,548)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from issuance of ordinary shares upon exercise of employee stock options	494	93	380
Proceeds from bank loan	—	25,000	25,000
Repayments of bank loan	—	—	(25,000)
Dividends paid	(20,765)	(22,899)	(32,120)
Net cash provided by (used in) financing activities	<u>(20,271)</u>	<u>2,194</u>	<u>(31,740)</u>
<b>NET INCREASE (DECREASE) IN CASH, CASH EQUIVALENTS, AND RESTRICTED</b>			
<b>CASH</b>	(12,783)	119,542	57,593
<b>EFFECT OF EXCHANGE RATE CHANGES</b>	(953)	(521)	2,753
<b>CASH, CASH EQUIVALENTS, AND RESTRICTED CASH, BEGINNING OF YEAR</b>	<u>215,892</u>	<u>202,156</u>	<u>321,177</u>
<b>CASH, CASH EQUIVALENTS, AND RESTRICTED CASH, END OF YEAR</b>	<u><u>202,156</u></u>	<u><u>321,177</u></u>	<u><u>381,523</u></u>
<b>SUPPLEMENTAL INFORMATION</b>			
Interest paid	6	105	367
Income taxes paid	<u>20,494</u>	<u>24,300</u>	<u>30,910</u>

	<u>Year Ended December 31</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
	As Adjusted (Note 2) US\$	(Note 2) US\$	(Note 2) US\$
Acquisition of Shannon Systems (Note 3)			
Fair value of assets acquired, net of cash, cash equivalents, and restricted cash acquired . . . .	43,661	—	—
Other long-term liabilities . . . . .	(5,735)	—	—
Issuance of stock . . . . .	<u>(7,640)</u>	—	—
Cash paid for business acquisition, net of cash, cash equivalents, and restricted cash acquired . . . . .	<u>30,286</u>	<u>—</u>	<u>—</u>
Acquisition of Bigtera (Note 3)			
Fair value of assets acquired, net of cash, cash equivalents, and restricted cash acquired . . . .	—	—	4,586
Other current liabilities . . . . .	—	—	(1,244)
Other long-term liabilities . . . . .	<u>—</u>	<u>—</u>	<u>(477)</u>
Cash paid for business acquisition, net of cash, cash equivalents, and restricted cash acquired . . . . .	<u>—</u>	<u>—</u>	<u>2,865</u>

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



**SILICON MOTION TECHNOLOGY CORPORATION AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(In Thousands)**

**1. ORGANIZATION AND OPERATIONS**

Silicon Motion Technology Corporation (“SMTC”, collectively with its subsidiaries the “Company”) is the global leader in supplying NAND flash controllers for solid state storage devices and the merchant leader in supplying SSD controllers. The Company has the broadest portfolio of controller technologies and solutions and ship over 750 million NAND controllers annually, more than any other company in the world. The Company’s controllers are widely used in embedded storage products such as SSDs and eMMCs which are found in smartphones, PCs and industrial and commercial applications. The Company also supply specialized high-performance hyperscale datacenter and industrial SSD solutions. The Company’s customers include most of the NAND flash vendors, storage device module makers and leading OEMs.

The Company acquired SMI Taiwan in April 2005. Originally SMI Taiwan was known as Feiya Technology Corporation (“Feiya”), a Taiwan corporation which was incorporated in April 1997 but had changed its name to SMI Taiwan after acquiring in August 2002 Silicon Motion, Inc., a California corporation (“SMI USA”), which was incorporated in November 1995. Feiya was originally a flash memory products company and SMI USA a graphics processor company. In April 2007, the Company acquired FCI, a leading designer of RF ICs for mobile TV and wireless communications based in South Korea. In July 2015, the Company acquired Shanghai Baocun Information Technology Co., Ltd. (“Shannon Systems”), China’s leading enterprise-class PCIe SSD company based in Shanghai, China. In July 2017, the Company acquired Bigtera, a software defined storage company.

**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 (U.S. GAAP). The consolidated financial statements include the accounts of SMTC and its wholly-owned subsidiaries. The Company owns 100% of the outstanding shares in all of its subsidiaries. All significant intercompany balances and transactions have been eliminated upon consolidation.

*Use of Estimates*

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. The actual results could differ from those estimates.

*Concentration of Credit Risk and Significant Customers*

Financial instruments that potentially subject the Company to a significant concentration of credit risk consist principally of cash equivalents, short term investments and accounts receivable. Cash, cash equivalents and short-term investments balances are maintained with high quality financial institutions, the composition and maturities of which are regularly monitored by management. The Company believes that the concentration of credit risk in its trade receivables, is substantially mitigated by the Company’s credit evaluation process, relatively short collection terms and the high level of credit worthiness of its customers. The Company performs ongoing credit evaluations of its customers’ financial conditions and limits the amount of credit extended based upon payment history and the customer’s current credit worthiness. The Company regularly reviews the allowance for bad debt and doubtful accounts by considering factors such as historical experience, credit quality, age of the accounts receivable balances and current economic conditions that may affect a customer’s ability to pay.

Historically, a relatively small number of customers have accounted for a significant portion of our net revenue. Sales to one customer in 2015 and 2016, and two customers in 2017 accounted for 10% or more of the Company's net sales, and these sales represented 30%, 28% and 39% of the Company's net sales in 2015, 2016 and 2017, respectively. In 2015 and 2016, the significant customer was SK Hynix and in 2017, SK Hynix and Intel. The Company's top ten customers in 2015, 2016 and 2017 accounted for approximately 72%, 75% and 72% of net sales, respectively.

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

The carrying amount of the Company's financial instruments, including cash and cash equivalents, notes and accounts receivable and notes and accounts payables approximates fair value due to the short-term maturity of the instruments. Fair values of short-term investments represent quoted market prices, if available. If no quoted market prices are available, fair values are estimated based on discounted cash flow, or other valuation techniques. Long-term investments in privately-held companies with no readily determinable market value are recorded using the cost method, since the cost of obtaining verifiable fair value is unreasonably high. 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 for that period. The Company's long-term liabilities approximate their fair values as they contain interest rates that vary according to market interest rates.

Fair value is the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that assets or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the Company. 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. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

Level 1 — Use unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 — Use observable inputs other than Level 1 prices such as quoted prices for identical or similar instruments in markets that are not active, quoted prices for similar instruments in active markets, and model-based valuation in which all significant inputs are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 — Use inputs that are generally unobservable and reflect the use of significant management judgments and estimates.

See Note 20, "Fair Value Measurement", for the related disclosure.

### ***Cash Equivalents***

The Company considers all highly liquid instruments acquired with a remaining maturity of three months or less when purchased to be cash equivalents. In addition, time deposits with maturities ranging from more than three months to one year are considered qualified as cash equivalents as the nature of the time deposits are similar to cash such that without advance notice to the bank, they can be readily converted into known amounts of cash with the principal of the time deposits protected and not subject to penalty in the event of an early withdrawal. Also, the risk of changes in value because of changes in interest rates is insignificant due to the fact that the Company can still earn interest based on a rate close to the on-going published interest rate applicable for the actual period of the time deposits in the event of an early withdrawal. Cash and cash equivalents are stated at cost, which approximates their fair value.

### ***Short-term Investments***

The Company's short-term investments primarily includes short-term income yielding investments with original maturities greater than three months from the purchase date and remaining maturities less than one year. These short-term investments consist mostly of bond funds and principal protected notes that are bought and held principally for the purpose of selling them in the near term and are classified as trading securities as well as senior notes classified as held-to-maturity investments with maturities less than one year. Trading securities are reported at fair value with the subsequent changes in fair value recorded in earnings as unrealized gains and losses. Senior notes are measured at amortized cost using the effective interest method less any impairment.

### ***Allowance for Doubtful Receivables***

An allowance for doubtful receivables is provided based on a review of the collectability of accounts receivables. The Company determines the amount of allowance for doubtful receivables by examining the historical collection experience and current trends in the credit quality of its customers as well as its internal credit policies.

### ***Inventories***

Inventories are stated at the lower of cost or market value. Inventories are recorded at standard cost and adjusted to the approximate weighted-average cost at the balance sheet date. Market value represents the current replacement cost for raw materials, work in process and finished goods. The Company assesses its inventory for estimated obsolescence or unmarketable inventory based upon management's assumptions about future demand and market conditions. In estimating reserves for obsolescence, the Company primarily evaluates estimates based on the timing of the introduction of new products and the quantities remaining of old products and provides reserves for inventory on hand in excess of the estimated demand. Estimated losses on slow-moving items are recognized and included in the allowance for losses.

### ***Long-term Investments***

The Company has long-term investments in companies that it does not exercise significant influence and accounts for these investments under the cost method. Management regularly evaluates financial information related to these investments to determine whether an other than temporary decline in their value exists. Factors indicative of an other than temporary decline include recurring operating losses, credit defaults and subsequent rounds of financings at an amount below the cost basis of the investment. Management periodically weighs all quantitative and qualitative factors in determining if any impairment loss exists. When a decline in value is deemed to be other-than-temporary, the Company recognizes an impairment loss in other income and expense.

### ***Noncurrent Assets Held for Sale***

Non-current assets are presented separately as held for sale when the Company is committed to selling the asset, an active plan of sale has commenced, and the sale is expected to be completed within 12 months. Assets held for sale are measured at the lower of their carrying amount and fair value less cost to sell. Assets held for sale are no longer amortized or depreciated.

### ***Property and Equipment***

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

Depreciation is computed using the straight-line method over estimated useful lives that range as follows: buildings — 25 to 50 years; machinery and equipment — 3 to 6 years; furniture and fixtures — 3 to 8 years;

software — 1 to 5 years; leasehold and buildings improvement — the shorter of the estimated useful life or lease term, which is generally 2 to 6 years. Depreciation expense recognized for the years ended December 31, 2015, 2016 and 2017 was approximately US\$7,936 thousand, US\$9,482 thousand and US\$10,599 thousand, respectively.

Upon the sale or other disposal of property and equipment, the related cost and accumulated depreciation are removed from the accounts, and any gain or loss is credited or charged to operating income.

### ***Government Grants***

Grants received by the Company from the Korean government to assist with specific research and development activities are deducted from those research and development costs incurred, in the period in which the related expenses are incurred, to the extent that they are non-refundable. Government grants that were used for the acquisition of fixed assets are deducted from the acquisition costs of the acquired assets and amortized over the useful lives of the related assets. The Company recognizes refundable government grants as long-term payable and current portion of long-term payable on its consolidated balance sheet.

### ***Goodwill and Intangible Assets***

Goodwill is the excess of the purchase price paid over the fair value of the net tangible and intangible assets acquired in a business combination. Intangible assets, which consist primarily of development technology, are amortized over their estimated useful lives, of 3.5 to 5.5 years.

### ***Impairment of Goodwill and Long-Lived Assets***

The Company evaluates the recoverability of long-lived assets whenever events or changes in circumstances indicate the carrying value may not be recoverable. The determination of recoverability is based on an estimate of undiscounted cash flows expected to result from the use of an asset and its eventual disposition. The estimate of cash flows is based upon, among other things, certain assumptions about expected future operating performance, growth rates and other factors. Estimates of undiscounted cash flows may differ from actual cash flows due to, among other things, technological changes, economic conditions, changes to the business model or changes in operating performance. If the sum of the undiscounted cash flows is less than the carrying value, an impairment loss is recognized, measured as the amount by which the carrying value exceeds the fair value of the asset. Fair value is determined by reference to quoted market prices, if available, or discounted cash flows, as appropriate. See Note 11, “Goodwill and Acquired Intangible Assets,” regarding impairment testing in fiscal year 2015, 2016 and 2017.

The Company monitors the recoverability of goodwill recorded in connection with acquisitions, by reporting unit, annually, or sooner if events or changes in circumstances indicate that the carrying amount may not be recoverable. The Company conducts its annual impairment test of goodwill on November 30. Reporting units may be operating segments as a whole or an operation one level below an operating segment, referred to as a component. Prior to fiscal 2017, goodwill impairment is tested using a two-step approach. The first step compares the fair value of a reporting unit to its carrying amount, including goodwill. If the fair value of the reporting unit is greater than its carrying amount, goodwill is not considered impaired and the second step is not required. If the fair value of the reporting unit is less than its carrying amount, the second step of the impairment test measures the amount of the impairment loss, if any, by comparing the implied fair value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recognized equal to that excess. The implied fair value of goodwill is calculated in the same manner that goodwill is calculated in a business combination, whereby the fair value of the reporting unit is allocated to all of the assets and liabilities of that unit, with the excess purchase price over the amounts assigned to assets and liabilities.

In January 2017, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) 2017-04, which removes step two from the goodwill impairment test. The Company elected to early adopt this ASU in the fourth quarter of 2017, in conjunction with the Company’s annual review for impairment.

Estimating fair value is performed by utilizing various valuation approaches, such as income approach or market approach. The total of all reporting unit fair values was also compared to the Company’s market capitalization plus control premium for reasonableness. See Note 11, “Goodwill and Acquired Intangible Assets,” regarding impairment testing.

#### ***Other Assets***

Other assets primarily consist of industrial property right and deposits for office leases.

#### ***Restricted Assets***

Restricted assets consist of deposits required for litigation and restricted cash. Restricted cash represents cash set aside as collateral for obtaining capacity and borrowings as well as cash received from government grants with restriction on its usage.

#### ***Bank loans***

Loans from financial institutions are stated at the amount of unpaid principal. Bank loans comprise borrowings which are held by banks based in Taiwan.

#### ***Other long-term liabilities***

Other long-term liabilities primarily consist of payable to former shareholders of Shannon Systems and unrecognized tax benefit.

#### ***Pension Costs***

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

#### ***Revenue Recognition***

Revenue from product sales is generally recognized upon shipment to the customer provided that the Company has received a signed purchase order, the price is fixed or determinable, transfer of title has occurred in accordance with the shipping terms specified in the arrangement with the customer, collectibility from the customer is considered reasonably assured, product returns are reasonably estimable and there are no remaining significant obligations or customer acceptance requirements. Revenue on development service orders is generally recognized upon completion and customer acceptance of contractually agreed milestones.

The Company grants certain distributors limited rights of return and price protection rights on unsold products. The return rights are generally limited to five percent of the monetary value of products purchased within the preceding six months, provided that the distributor places a corresponding restocking order of equal or greater value. An allowance for sales returns for distributors and all customers is recorded at the time of sale based on historical returns information available, management’s judgment and any known factors at the time the financial statements are prepared that would significantly affect the allowance. Price protection rights are based on the inventory products the distributors have on hand at the date the price protection is offered. A reserve for price adjustments is recorded based on the estimated products on hand at the distributors and historical experience. The actual price adjustments to distributors incurred by the Company are minimal.

The Company provides a warranty period of one year for manufacturing defects of its products. Warranty returns have been infrequent and relate to defective or off-specification parts. The Company estimates a reserve for warranty based on historical experience and records this amount to cost of sales. For the years ended December 31, 2015, 2016 and 2017, the Company did not experience significant costs associated with warranty returns.

### ***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 that will be useful in developing new products or at significantly enhancing existing products as well as expenditures incurred for the design and testing of product alternatives. All expenditures related to research and development activities of the Company are charged to operating expenses when incurred. Third-party research and development costs are expensed when the contracted work has been performed or as milestone results have been achieved.

### ***Income Taxes***

The provision for income tax represents income tax paid and payable for the current year plus changes in the deferred income tax assets and liabilities during the years. Deferred income tax assets are recognized for net operating loss carryforwards, research and development credits, and temporary differences. 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 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. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company records interest and penalties related to unrecognized tax benefits in income tax expense.

### ***Foreign Currency Transactions***

Foreign currency transactions are recorded at the rates 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 receivables and payables are settled, are credited or charged to income in the period of conversion or settlement. At the balance sheet date, assets and liabilities denominated in foreign currencies are remeasured 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 U.S. dollars. The functional currency of some of the Company's subsidiaries is the local currency of the respective entity. Accordingly, the financial statements of the foreign subsidiaries were translated into U.S. dollars at the following exchange rates: assets and liabilities — current rate on the balance sheet date; shareholders' equity — historical rates; income and expenses — average rate during the period. The resulting translation adjustment is recorded as a separate component of comprehensive income.



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

Comprehensive income and loss represents net income (loss) plus the results of certain changes in shareholders' equity during a period from non-owner sources. The following table presents the components of accumulated other comprehensive income (loss) as of December 31, 2015, 2016 and 2017:

	Year Ended December 31, 2015			Year Ended December 31, 2016			Year Ended December 31, 2017		
	US\$			US\$			US\$		
	Foreign currency items	Defined benefit pension plans	Accumulated other comprehensive income (loss)	Foreign currency items	Defined benefit pension plans	Accumulated other comprehensive income (loss)	Foreign currency items	Defined benefit pension plans	Accumulated other comprehensive income (loss)
Beginning balance . . .	3,354	(849)	2,505	1,486	(853)	633	(69)	(963)	(1,032)
Current-period change . . . . .	(1,868)	(4)	(1,872)	(1,555)	(110)	(1,665)	3,390	285	3,675
Ending balance . . . . .	<u>1,486</u>	<u>(853)</u>	<u>633</u>	<u>(69)</u>	<u>(963)</u>	<u>(1,032)</u>	<u>3,321</u>	<u>(678)</u>	<u>2,643</u>

### ***Legal Contingencies***

The Company is regularly 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. Because 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.

### ***Earnings Per Share***

Basic earnings per share are computed by dividing net earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period. Diluted earnings per share reflect the potential dilution that could occur if stock options and other dilutive securities were exercised. Dilutive securities are excluded from the computation of the diluted income per share in periods when their effect is anti-dilutive. The Company's dilutive securities consist of employee stock options and restricted stock units. The effect of dilutive securities including employee stock options and restricted stock units were 1,534 thousand shares (384 thousand ADSs), 1,131 thousand shares (283 thousand ADSs) and 868 thousand shares (218 thousand ADSs) for the years ended December 31, 2015, 2016 and 2017, respectively.

### ***Stock-Based Compensation***

The Company accounts for stock-based compensation in accordance with ASC 718 Compensation — Stock Compensation. The Company uses the Black-Scholes valuation model for the valuation of stock options and recognizes compensation expense on a straight-line basis over the requisite service period of the award. The value of our restricted stock units is based on the fair value of our shares on the date of grant and expensed over the vesting period.

Prior to the initial declaration of a quarterly cash dividend on January 22, 2013, the fair value of restricted stock units ("RSUs") was measured based on the grant date share price, as the Company did not historically pay cash dividends on our common stock. For awards granted on or subsequent to January 22, 2013, the fair value of RSUs was measured based on the grant date share price, less the present value of expected dividends during the vesting period, discounted at a risk-free interest rate.

## ***Dividends***

Our Board of Directors declared payment of our first quarterly dividend on our common stock in January 2013 and the first dividend payment was made on March 4, 2013. Our Board of Directors has subsequently declared and paid dividends in each successive quarter. On October 24, 2016 and October 24, 2017, our Board of Directors, instead of declaring a quarterly dividend, declared an annual dividend payable in four quarterly installments. The payment of future cash dividends are subject to the Board's continuing determination that the payment of dividends are in the best interests of the Company's shareholders and are in compliance with all laws and agreements of the Company applicable to the declaration and payment of cash dividends.

## ***Recent Accounting Pronouncements***

In May 2014, the 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 will adopt this new standard as of January 1, 2018, using the modified retrospective method with the cumulative effect of initially applying it recognized at the date of initial application. The Company has finalized its assessment and has identified that the adoption of this new standard will not have a material impact on the Company's financial position, results of operations, cash flow and financial statement disclosures.

In April 2015, the FASB issued an accounting update regarding the measurement date of a defined benefit obligation and plan assets. The amendment permits the entity with a fiscal year-end that does not coincide with a month-end to measure defined benefit plan assets and obligations using the month-end that is closest to the entity's fiscal year-end. If a contribution or significant event (such as a plan amendment, settlement, or curtailment that calls for a remeasurement in accordance with existing requirements) occurs between the month-end date used to measure defined benefit plan assets and obligations and an entity's fiscal year-end, the entity should adjust the measurement of defined benefit plan assets and obligations to reflect the effects of those contributions or significant events. This amendment is effective for fiscal years beginning after December 15, 2016 and early application 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 did not 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 elected to have an early adoption of the amendment as of December 31, 2015, and the adoption of this amendment did not have a material impact on the Company's financial position.

In February 2016, the FASB issued a new standard regarding leases (Topic 842). 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. In January 2018, the FASB issued an amendment that permits an entity to elect an optional transition practical expedient to not evaluate under Topic 842 land easements that exist or expired before the entity's adoption of Topic 842 and that were not previously accounted for as leases under Topic 840, the current standard regarding leases. The guidance 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 did not 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 statement of cash flows.

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 Company is currently evaluating the impact that the adoption will have on its statement of cash flows.

In October 2016, the FASB issued an accounting update to simplify the accounting for the income tax consequences of intra-entity transfers of assets other than inventory. The amendment removes the prohibition against the recognition of current and deferred income tax effects of intra-entity transfers of assets other than

inventory until the asset has been sold to an outside party. The amendment is effective for fiscal years beginning after December 15, 2017, 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 October 2016, the FASB issued an accounting update to amend the consolidation guidance on how a reporting entity that is the single decision maker of a variable interest entity ("VIE") should treat indirect interests in the entity held through related parties that are under common control with the reporting entity when determining whether it is the primary beneficiary of that VIE. Under this amendment, the single decision maker is required to consider that indirect economic interests in the VIE held through related parties that are under common control on a proportionate basis. However, this amendment does not change the existing characteristics of a primary beneficiary. The amendment is effective for fiscal years beginning after December 15, 2016, and earlier adoption is permitted. The adoption of this amendment did not have a material impact on the Company's financial position, results of operations, cash flow and financial statement disclosures.

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 has elected to adopt the amendment as of December 31, 2016, and the retrospective transition approach is applied to prior reporting periods presented. The adoption of this amendment did not have a material impact on the Company's financial position.

The following table reflects the adjustments made to the consolidated statements of cash flows to confirm prior period classifications under the new guidance for the periods presented:

	<u>As Reported</u>	<u>Adjustment</u>	<u>As Adjusted</u>
	US\$	US\$	US\$
Year Ended December 31, 2014:			
Net cash provided by operating activities . . . .	68,725	—	68,725
Net cash provided by (used in) investing activities . . . . .	(15,413)	3,817	(11,596)
Net cash used in financing activities . . . . .	<u>(19,710)</u>	<u>—</u>	<u>(19,710)</u>
Net increase (decrease) in cash, cash equivalents, and restricted cash* . . . . .	33,602	3,817	37,419
Effect of exchange rate changes . . . . .	(1,111)	—	(1,111)
Cash, cash equivalents, and restricted cash* at beginning of year . . . . .	<u>161,720</u>	<u>17,864</u>	<u>179,584</u>
Cash, cash equivalents, and restricted cash* at end of year . . . . .	<u><u>194,211</u></u>	<u><u>21,681</u></u>	<u><u>215,892</u></u>
Year Ended December 31, 2015:			
Net cash provided by operating activities . . . .	65,946	—	65,946
Net cash used in investing activities . . . . .	(58,414)	(44)	(58,458)
Net cash used in financing activities . . . . .	<u>(20,271)</u>	<u>—</u>	<u>(20,271)</u>
Net increase (decrease) in cash, cash equivalents, and restricted cash* . . . . .	(12,739)	(44)	(12,783)
Effect of exchange rate changes . . . . .	(953)	—	(953)
Cash, cash equivalents, and restricted cash* at beginning of year . . . . .	<u>194,211</u>	<u>21,681</u>	<u>215,892</u>
Cash, cash equivalents, and restricted cash* at end of year . . . . .	<u><u>180,519</u></u>	<u><u>21,637</u></u>	<u><u>202,156</u></u>

\* The restricted cash is only included in the amount of “as adjusted” item.

To early adopt the accounting update, the Company has amended the presentation of changes in cash and cash equivalents by explaining the changes in the total of cash, cash equivalents, and restricted cash. The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the consolidated balance sheets that sum to the total of the same such amounts shown in the statement of cash flows.

	<u>As of December 31</u>			
	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
	US\$	US\$	US\$	US\$
Cash and cash equivalents . . . . .	194,211	180,519	274,483	359,453
Restricted cash included in restricted assets-current . . . . .	19,322	19,328	44,393	19,515
Restricted cash included in other assets . . . . .	<u>2,359</u>	<u>2,309</u>	<u>2,301</u>	<u>2,555</u>
Total cash, cash equivalents, and restricted cash shown in the statements of cash flows . . . . .	<u><u>215,892</u></u>	<u><u>202,156</u></u>	<u><u>321,177</u></u>	<u><u>381,523</u></u>

Amounts included in restricted cash represent (a) cash and time deposits set aside as collateral for obtaining capacity; (b) cash received from government grants with restriction on its usage; and (c) cash and time deposits that are pledged for short-term loans.

In January 2017, the FASB issued an accounting update to clarify the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or

businesses. The amendment provides a screen to determine when an integrated set of assets and activities (collectively referred to as a “set”) is not a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. If the screen is not met, the amendment requires that to be considered a business, a set must include an input and a substantive process that together significantly contribute to the ability to create output. The amendment is effective for fiscal years beginning after December 15, 2017. The Company is currently evaluating the impact that the adoption will have on its results of operations, financial position, cash flow and disclosures.

In January 2017, the FASB issued an accounting update to simplify the accounting treatment for the impairment of goodwill. The amendment eliminates Step 2 from the goodwill impairment test, which measures a goodwill impairment loss by calculating the implied fair value of goodwill by assigning the fair value of a reporting unit to all of its assets and liabilities as if that reporting unit had been acquired in a business combination. Instead, under this amendment, the entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value and the impairment loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The amendment is effective for fiscal years beginning after December 15, 2019, and early adoption is permitted. The Company adopted this amendment beginning in fiscal 2017 and performed the annual goodwill impairment test in accordance with the amended guidance. Refer to Note 11 for discussion of the annual goodwill impairment test.

In February 2017, the FASB issued an accounting update to clarify the scope of asset derecognition guidance and accounting for partial sales of nonfinancial assets. The amendment defines the term “in substance nonfinancial asset” as a financial asset promised to counterparty in a contract if substantially all of the fair value of assets (recognized and unrecognized) that are promised to the counterparty in the contract is concentrated in nonfinancial assets and clarifies that an entity should identify each distinct nonfinancial asset or in substance nonfinancial asset promised to a counterparty and derecognize each asset when a counterparty obtains control of it. The amendment also clarifies that an entity should allocate consideration to each distinct asset by applying the guidance in Topic 606 on allocating the transaction price to performance obligations. Under this amendment, an entity is required to derecognize a distinct nonfinancial asset or distinct in substance nonfinancial asset in a partial sale transaction when it (1) does not have (or ceases to have) a controlling financial interest in the legal entity that holds the asset in accordance with Topic 810 and (2) transfers control of the asset in accordance with Topic 606. Once an entity transfers control of a distinct nonfinancial asset or distinct in substance nonfinancial asset, it is required to measure any noncontrolling interest it receives (or retains) at fair value. The amendment is effective for fiscal years beginning after December 15, 2017 and early adoption is permitted. The amendment should be applied on a full or modified retrospective basis. 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 March 2017, the FASB issued an accounting update to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost. The amendment requires that an entity disaggregates the service cost component from the other components of net benefit cost and present the service cost component with other current compensation costs for related employees in the income statement. The amendment also requires an entity presents the other components elsewhere in the income statement and outside of income from operation if such subtotal is presented and allow only the service cost component of net benefit cost to be eligible for capitalization. The amendment is effective for fiscal years beginning after December 15, 2017 and early adoption is permitted. The amendment should be applied retrospectively for the presentation of the service cost component and the other components of net periodic pension cost and net periodic postretirement benefit cost in the income statement and prospectively, on and after the effective date, for the capitalization of the service cost component of net periodic pension cost and net periodic postretirement benefit in assets. The amendment allows for a practical expedient that permits an entity to use the amounts disclosed in its pension and other postretirement benefit plan note for the prior comparative periods as the estimation basis for applying the retrospective presentation requirements. The Company intends not to apply the practical expedient for apply the retrospective



presentation requirements. 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 May 2017, the FASB issued an accounting update to provide clarity and reduce both (1) diversity in practice and (2) cost and complexity when applying the guidance in Topic 718, Compensation—Stock Compensation, to a change in the terms or conditions of a share-based payment award. Under the amendment, modification accounting is required to be applied unless all of the following are the same immediately before and after the change: (1) the award's fair value (or calculated value or intrinsic value, if those measurement methods are used); (2) the award's vesting conditions; and (3) the award's classification as an equity or liability instrument. The amendment is effective for fiscal years beginning after December 15, 2017 and early adoption is permitted. The amendment should be applied prospectively to an award modified on or after the adoption date. 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.

### 3. BUSINESS ACQUISITION

#### *Shannon*

On July 1, 2015, the Company completed its acquisition of Shannon Systems, China's leading enterprise-class PCIe SSD company based in Shanghai, China. In exchange for 100% of the outstanding shares of common stock of Shannon Systems, the Company issued 1,560 thousand ordinary shares with fair value of US\$7,640 thousand and paid approximately US\$37,925 thousand in cash. The value of the 1,560 thousand ordinary shares issued was determined based on the market value of the Company's common shares at the date of the acquisition, discounted for the fact that the shares are restricted as to their marketability for a period of five years from the issuance date. In 2015, the Company incurred US\$359 thousand of acquisition costs which comprised primarily of transaction fees and direct acquisition costs, including legal, accounting, and other professional fees. These costs are included in the line item of "operating expenses—general and administrative" on the consolidated statements of income.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition:

	US\$
Cash, cash equivalents and restricted cash . . . . .	1,904
Accounts receivable, net . . . . .	946
Inventories . . . . .	2,624
Other current assets . . . . .	288
Property and equipment . . . . .	71
Goodwill . . . . .	33,204
Identifiable intangible assets . . . . .	8,381
Accounts payable . . . . .	(644)
Accrued expenses and other current liabilities . . . . .	<u>(1,209)</u>
Net assets acquired . . . . .	<u>45,565</u>

As of December 31, 2017, approximately US\$5,735 thousand has not been paid to the former shareholders of Shannon Systems and is included in other long-term liabilities on the consolidated balance sheets as of both December 31, 2016 and 2017.

The excess of the purchase price over the fair value of the net tangible assets acquired has been reflected as identifiable intangible assets. The identifiable intangible assets and respective useful lives are as follows:

	US\$	Useful Life
Developed technology . . . . .	3,789	3.5
In-process research and development (“IPR&D”) . . . . .	<u>4,592</u>	indefinite
Total identifiable intangible assets . . . . .	<u>8,381</u>	

Developed technology represented the existing know-how in enterprise-class PCIe SSD including all the developed and in-process products for the Shannon Systems business.

The estimated fair value of IPR&D was defined as research and development projects related to enterprise-class PCIe SSDs in-process at the time of the transaction that had not demonstrated their technological feasibility and that do not have an alternative future use.

Goodwill represents the excess of the purchase price over the estimated fair values of the net tangible and intangible assets. The factors that contributed to the recognition of goodwill primarily relate to expansion into new product areas and potential synergies created from combined capabilities, and goodwill is not expected to be deductible for tax purposes.

The results of Shannon Systems since the acquisition date included on the consolidated statement of income for the year ended December 31, 2015 were as follows:

	US\$
Net sales . . . . .	9,049
Net income . . . . .	421

The operating results of Shannon Systems have been included in the Company’s operations beginning July 1, 2015. The following unaudited pro forma information represents a summary of the results of operations as if the acquisition occurred on January 1, 2014 and 2015 and includes certain pro forma adjustments, including amortization of identifiable intangibles from that date (in thousands except earnings per share):

	<u>Year Ended December 31</u>	
	<u>2014</u>	<u>2015</u>
Net sales . . . . .	293,562	364,670
Net income . . . . .	42,483	58,468
Earnings per share		
Basic . . . . .	0.31	0.42
Diluted . . . . .	0.31	0.42
Weighted average ordinary shares outstanding (thousand)		
Basic . . . . .	136,164	138,880
Diluted . . . . .	138,347	140,414

The pro forma results are based on various assumptions and are not necessarily indicative of what would have occurred had the acquisition closed on January 1, 2014 and 2015.

***Bigtera***

On July 3, 2017, the Company completed its acquisition of Bigtera, a software defined storage company. In exchange for 100% of the outstanding shares of common stock of Bigtera, the Company paid approximately US\$4,664 thousand in cash. In 2017, the Company incurred US\$171 thousand of acquisition costs which comprised primarily of transaction fees and direct acquisition costs, including legal and other professional fees. These costs are included in the line item of “operating expenses—general and administrative” on the consolidated statements of income.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition:

	US\$
Cash, cash equivalents and restricted cash . . . . .	78
Accounts receivable, net . . . . .	380
Other current assets . . . . .	14
Property and equipment . . . . .	15
Goodwill . . . . .	625
Identifiable intangible assets . . . . .	4,736
Accounts payable . . . . .	(436)
Accrued expenses and other current liabilities . . . . .	<u>(748)</u>
Net assets acquired . . . . .	<u>4,664</u>

As of December 31, 2017, approximately US\$1,721 thousand has not been paid to the former shareholders of Bigtera and is included in other current and long-term liabilities on the consolidated balance sheets as of December 31, 2017.

The excess of the purchase price over the fair value of the net tangible assets acquired has been reflected as identifiable intangible assets. The identifiable intangible assets and respective useful lives are as follows:

	US\$	Useful Life
Know-how . . . . .	3,753	5.5
Current technology . . . . .	<u>983</u>	5.5
Total identifiable intangible assets . . . . .	<u>4,736</u>	

Know-how represents software device storage (SDS) technology that has value through its continued use or reuse across all version of Bigtera’s software products. Such know-how derives independent value from not being generally known and is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

Current technology represents the part of technology that is unique in current version of software products.

Goodwill represents the excess of the purchase price over the estimated fair values of the net tangible and intangible assets. The factors that contributed to the recognition of goodwill primarily relate to expansion into new product areas and potential synergies created from combined capabilities, and goodwill is not expected to be deductible for tax purposes.

The results of Bigtera since the acquisition date included on the consolidated statement of income for the year ended December 31, 2017 were as follows:

	US\$
Net sales . . . . .	2,993
Net income . . . . .	(314)

The operating results of Bigtera have been included in the Company's operations beginning July 3, 2017. The following unaudited pro forma information represents a summary of the results of operations as if the acquisition occurred on January 1, 2016 and 2017 and includes certain pro forma adjustments, including amortization of identifiable intangibles from that date (in thousands except earnings per share):

	<u>Year Ended December 31</u>	
	<u>2016</u>	<u>2017</u>
Net sales .....	557,672	523,849
Net income .....	109,736	73,834
Earnings per share		
Basic .....	0.78	0.52
Diluted .....	0.77	0.51
Weighted average ordinary shares outstanding (thousand)		
Basic .....	140,919	142,738
Diluted .....	142,050	143,606

The pro forma results are based on various assumptions and are not necessarily indicative of what would have occurred had the acquisition closed on January 1, 2016 and 2017.

#### 4. CASH, CASH EQUIVALENTS, AND RESTRICTED CASH

	<u>December 31</u>	
	<u>2016</u>	<u>2017</u>
	US\$	US\$
Cash and deposits in bank .....	58,391	59,751
Time deposits .....	199,064	269,392
Bonds acquired under repurchase agreements .....	17,028	30,310
Total cash and cash equivalents .....	274,483	359,453
Restricted cash (Note 2) .....	46,694	22,070
	<u>321,177</u>	<u>381,523</u>

#### 5. SHORT-TERM INVESTMENTS

	<u>December 31</u>	
	<u>2016</u>	<u>2017</u>
	US\$	US\$
Trading securities .....	3,302	6,941

The Company classified certain short-term investments as trading securities. Realized gains on sales of these trading securities were US\$3 thousand, US\$2 thousand and US\$103 thousand for the years ended December 31, 2015, 2016 and 2017, respectively. The amount of unrealized losses related to trading securities at year end was nil for the years ended December 31, 2015, 2016 and 2017, respectively.

## 6. NOTES AND ACCOUNTS RECEIVABLE

	<u>December 31</u>	
	<u>2016</u>	<u>2017</u>
	US\$	US\$
Trade accounts receivable . . . . .	75,946	81,165
Allowance for doubtful accounts . . . . .	(723)	(598)
Allowance for sales returns and discounts . . . . .	(1,624)	(1,432)
	<u>73,599</u>	<u>79,135</u>

The changes in the allowances are summarized as follows:

	<u>Year Ended December 31</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
	US\$	US\$	US\$
Allowances for doubtful accounts			
Balance, beginning of year . . . . .	1,167	775	723
Reversals charged to expense, net . . . . .	(392)	(12)	(125)
Write-offs . . . . .	—	(40)	—
Balance, end of year . . . . .	<u>775</u>	<u>723</u>	<u>598</u>

	<u>Year Ended December 31</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
	US\$	US\$	US\$
Allowances for sales returns and discounts			
Balance, beginning of year . . . . .	1,427	1,555	1,624
Additions charged to expense, net . . . . .	1,753	3,285	3,093
Actual sales return and discount . . . . .	(1,625)	(3,216)	(3,285)
Balance, end of year . . . . .	<u>1,555</u>	<u>1,624</u>	<u>1,432</u>

## 7. INVENTORIES

The components of inventories are as follows:

	<u>December 31</u>	
	<u>2016</u>	<u>2017</u>
	US\$	US\$
Finished goods . . . . .	24,782	41,365
Work in process . . . . .	31,185	25,090
Raw materials . . . . .	15,920	27,731
	<u>71,887</u>	<u>94,186</u>

The Company wrote down US\$2,525 thousand, US\$2,995 thousand and US\$698 thousand in 2015, 2016 and 2017, respectively, for estimated obsolete or unmarketable inventory.

## 8. LONG-TERM INVESTMENTS

As of December 31, 2016 and 2017, the Company held equity investments in several privately-held companies with the carrying value as follows:

	Percentage of Ownership		December 31	
	2016	2017	2016 US\$	2017 US\$
Cost method:				
Cashido Corp. (Cashido) . . . . .	2.1%	2.1%	91	—
Vastview Technology, Corp. (Vastview) . . . . .	2.9%	2.9%	29	—
			120	—

In July 2001, the Company invested in the common stock of Cashido. At the time of investment, Cashido manufactured flash memory storage devices. Cashido currently focuses on the manufacture of computer accessories and ozone based sterilization devices. In 2016 and 2017, the Company recognized impairment charges of US\$13 thousand and US\$91 thousand in its investment in Cashido, respectively.

In December 2006 and February 2007, the Company invested US\$3,360 thousand in the common stock of Vastview. Vastview is a fabless semiconductor company that develops and markets driver ICs and other ICs for the TFT-LCD industry. In 2009 and 2013, the Company received US\$808 thousand and US\$46 thousand from capital reductions at Vastview. From 2008 to 2010, the Company recognized impairment charges of US\$2,462 thousand in its investment in Vastview, and an additional charge of US\$29 thousand in 2017. The impairment charges were mainly due to the declining financial performances of the investees.

The Company accounts for these investments using the cost method. These investments are evaluated for impairment on an annual basis or as circumstances warrant.

## 9. NONCURRENT ASSETS HELD FOR SALE

	December 31	
	2016 US\$	2017 US\$
Assets held for sale . . . . .	3,363	—
	3,363	—

The Company vacated from an office building located in Shanghai, China and in 2016 took action to sell the property. The sale plan met all of the held-for-sale criteria in accordance with ASC 360—Property, Plant and Equipment and the asset was reclassified accordingly. In 2017, the Company sold the property to a non-affiliated third party and recognized a gain from disposal of US\$1,880 thousand.



## 10. PROPERTY AND EQUIPMENT

	December 31	
	2016	2017
	US\$	US\$
Cost:		
Land . . . . .	9,309	9,309
Buildings . . . . .	29,232	30,288
Machinery and equipment . . . . .	18,122	21,665
Furniture and fixtures . . . . .	6,760	7,746
Leasehold and buildings improvement . . . . .	4,911	5,497
Software . . . . .	22,745	24,864
Total . . . . .	<u>91,079</u>	<u>99,369</u>
Accumulated depreciation:		
Buildings . . . . .	2,708	3,472
Machinery and equipment . . . . .	14,032	15,665
Furniture and fixtures . . . . .	4,207	5,212
Leasehold and buildings improvement . . . . .	3,591	4,213
Software . . . . .	<u>19,130</u>	<u>19,874</u>
	43,668	48,436
Prepayment and construction in progress . . . . .	<u>481</u>	<u>437</u>
	<u>47,892</u>	<u>51,370</u>

In April 2006, the Company began leasing a property located in Taipei, Taiwan to a third party. The lessee has been renewing the operating lease annually and last renewed in March 2018. Net carrying value of the properties as of December 31, 2016 and 2017 was US\$728 thousand and US\$709 thousand, respectively. Annual rental income from the lease is about US\$42 thousand each year.

## 11. GOODWILL AND ACQUIRED INTANGIBLE ASSETS

**Intangible assets:** The intangible assets acquired from the Company's acquisition of FCI and Centronix in 2007, BTL in 2011, Shannon Systems in 2015 and Bigtera in 2017 are as follows:

	December 31							
	2016				2017			
	US\$				US\$			
	Cost	Accumulated Impairment	Accumulated Amortization	Net Carrying Amount	Cost	Accumulated Impairment	Accumulated Amortization	Net Carrying Amount
Acquisition-related intangible assets . . . . .	8,381	—	(3,154)	5,227	13,117	—	(5,688)	7,429

No impairment losses were recognized in 2015, 2016 and 2017. Amortization expense of acquisition-related intangible assets for the years ended December 31, 2015, 2016 and 2017 were US\$1,051 thousand, US\$2,103 thousand and US\$2,534 thousand, respectively.

**Goodwill:** Goodwill is not amortized, but instead is reviewed and tested for impairment at least annually and whenever events or circumstances occur which indicate that goodwill might be impaired. The goodwill that resulted from the Company's acquisition of FCI and Centronix in 2007 and purchased of BTL's assets in 2011 was US\$66,300 thousand. As a result of the acquisition of Shannon Systems in 2015 and Bigtera in 2017, the

Company recorded additional goodwill of US\$33,204 thousand and US\$625 thousand, respectively. Impairment of goodwill is tested at the Company's reporting unit level by comparing the carrying amount, including goodwill, to the fair value. In performing the analysis, the Company uses the best information available, including reasonable and supportable assumptions and projections. Goodwill is tested for impairment annually on November 30. Total goodwill was US\$68,656 thousand and US\$58,964 thousand as of December 31, 2016 and 2017, respectively. The Company recognizes an impairment charge for the amount by which the carrying amount of the reporting unit exceeds its implied fair value. For the year ended December 31, 2017, the Company has elected to adopt ASU 2017-04 (as described in note 2 above). Under the updated guidance, the Company applied a one-step quantitative test and recorded the amount of goodwill impairment as the excess of a reporting unit's carrying amount over its fair value. Fair value determinations are sensitive to changes in the underlying assumptions and factors including those relating to estimating future operating cash flows to be generated from the reporting unit which are dependent upon historical data and internal forecasts and projections developed by management. The Company's strategic plans, estimates of perpetual growth rate taking into account the annual goodwill impairment analysis of the current economic environment and the timing and degree of any economic recovery and market participant assumptions. Key assumptions within the five-year discounted cash flow analysis prepared for the annual goodwill impairment analysis included revenue growth rates, projected gross margins, perpetual growth rate and risk-adjusted discount rate that the Company determined to be appropriate. The inputs used are classified as Level 3 within the fair value hierarchy due to the significance of unobservable inputs using company-specific information. As a result of the goodwill impairment test conducted as of November 30, 2017, the Company determined that the carrying amounts for mobile communication unit exceed its fair value and recorded a goodwill impairment charge of US\$10,337 thousand in the fourth quarter of 2017. The company used an income approach (discounted cash flow model) to determine the fair value of the mobile communication unit. The impairment charge was mainly attributable to a new project cancellation by a customer and delayed commercialization of a new product.

	December 31							
	2016				2017			
	US\$				US\$			
	Cost	Accumulated Impairment	Foreign Currency Adjustment	Net Carrying Amount	Cost	Accumulated Impairment	Foreign Currency Adjustment	Net Carrying Amount
Goodwill . . . . .	99,504	(30,808)	(40)	68,656	100,129	(41,145)	(20)	58,964

## 12. SHORT-TERM BANK LOANS

	December 31	
	2016	2017
	US\$	US\$
Secured loans . . . . .	25,000	25,000
	<u>25,000</u>	<u>25,000</u>

The interest expenses for the years ended December 31, 2015, 2016 and 2017 were nil, US\$105 and US\$387 thousand, respectively.

In 2016 and 2017, the Company obtained US dollar revolver credit facilities from two banks and drew down US\$25,000 thousand in 2016 and 2017, respectively. Interest rates ranged from 0.953% to 1.51% per annum on monthly outstanding loans. In 2016, loans were secured by US\$25 million of pledged deposits, which were recorded as current restricted cash, and in 2017, loans no longer required pledged deposits. The US\$25 million of loans is expected to be repaid in 2018.

### 13. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

	December 31	
	2016	2017
	US\$	US\$
Wages and bonus .....	29,028	29,629
Dividends .....	21,382	32,451
Research and development payable .....	5,456	5,638
License fees and royalties .....	4,021	3,729
Professional fees .....	2,038	2,286
Equipment .....	492	1,844
Others .....	6,319	8,186
	<u>68,736</u>	<u>83,763</u>

### 14. PENSION PLAN

SMI Taiwan, the Company's largest operating company is a Taiwan registered company and subject to Taiwan's Labor Pension Act (the "Act"), which became effective on July 1, 2005, and the pension mechanism under the Act is deemed a defined contribution plan. The employees who were subject to the Labor Standards Law prior to July 1, 2005 could choose to be subject to the pension mechanism under the Act or continue to be subject to the pension mechanism under the Labor Standards Law. For those employees who were subject to the Labor Standards Law prior to July 1, 2005 and still work for the same company after July 1, 2005 and have chosen to be subject to the pension mechanism under the Act, their seniority as of July 1, 2005 were maintained. The Act prescribes that the rate of contribution by an employer to employees' pension accounts per month will not be less than 6% of each employee's monthly salary. According to the Act, SMI Taiwan made monthly contributions and recognized pension costs of US\$1,015 thousand, US\$1,272 thousand and US\$1,579 thousand for the years ended December 31, 2015, 2016 and 2017, respectively.

The Company provides a defined benefit plan to the employees of SMI Taiwan under the Labor Standards Law that offers benefits based on an employee's length of service and average monthly salary for the six-month period prior to retirement. The Company contributes an amount equal to 2% of salaries paid each month to a pension funds (the "Funds"), which is administered by the Labor Pension Fund Supervisory Committee established by the government (the "Committee") and deposited in the Committee's name in the Bank of Taiwan. Before the end of each year, the Company assesses the balance in the Funds. If the amount of the balance in the Funds is inadequate to pay retirement benefit for employees who conform to retirements in the next year, the Company is required to fund the difference in one appropriation that should be made before the end of March of the next year. 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 2017, the asset allocation was primarily in cash, equity securities and debt securities. Furthermore, under the Labor Standards Law, the rate of return on assets shall not be less than the average interest rate on a two-year time deposit published by the local banks. The government is responsible for any shortfall in the event that the rate of return is less than the required rate of return. 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 Company by the government. Therefore, the Company is unable to provide the required fair value disclosures related to pension plan assets. Future contributions will be based on 2% of the employee salaries at that time. The Company estimates its contribution for the year ending December 31, 2018 to be US\$69 thousand which was determined based on 2% of estimated salaries in 2018.

Starting in 2010, the Company provides a defined benefit pension plan to the Korean employees of FCI with at least one year of service. FCI's overall investment strategy is to avoid a negative return on plan assets. FCI estimates its contribution for the year ending December 31, 2018 to be nil.

For employees under defined contribution pension plans, pension costs are recorded based on the actual contributions made to employees' individual pension accounts. For employees under defined benefit pension plans, pension costs are recorded based on actuarial calculations. Determining the cost associated with such benefits is dependent on various actuarial assumptions, including discount rate, expected return on plan assets, compensation increase, employee mortality and turnover rates. The Company reviewed its actuarial assumptions at the measurement date on December 31 every year. The effect of modifications to assumptions is recorded in accumulated other comprehensive loss and amortized to net periodic cost over future periods using the corridor method. The Company believes that assumptions utilized in recording its obligations under its plans are reasonable based on its experience and market conditions. Independent actuaries perform the required calculations to determine expense in accordance with U.S. GAAP. Actual results may differ from the actuarial assumptions and are generally accumulated and amortized into earnings over future periods. The net periodic costs are recognized as employees render services necessary to earn the benefits.

The changes in benefits obligation and plan assets and the reconciliation of funded status are as follows:

	<b>December 31</b>		
	<b>2015</b>	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>	<b>US\$</b>
<b>Change in benefit obligation</b>			
Projected benefit obligation at beginning of year . . . . .	3,320	3,632	4,242
Service cost . . . . .	273	487	1,572
Interest cost . . . . .	57	104	336
Actuarial loss (gain) . . . . .	79	151	(665)
Benefits paid . . . . .	(97)	(132)	(354)
Projected benefit obligation at end of year . . . . .	<u>3,632</u>	<u>4,242</u>	<u>5,131</u>
<b>Change in plan assets</b>			
Fair value of plan assets at beginning of year . . . . .	2,556	2,800	3,902
Actual return on plan assets . . . . .	33	33	81
Employer contributions . . . . .	328	1,203	1,358
Benefits paid . . . . .	(117)	(134)	(227)
Fair value of plan assets at end of year . . . . .	<u>2,800</u>	<u>3,902</u>	<u>5,114</u>
Funded status recognized as an other asset (liabilities) . . . . .	<u>(832)</u>	<u>(340)</u>	<u>(17)</u>

Amounts recognized in accumulated other comprehensive income consist of the following:

	<b>Year Ended December 31</b>		
	<b>2015</b>	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>	<b>US\$</b>
Net loss . . . . .	852	963	678
Transition obligation . . . . .	1	—	—
Total recognized in accumulated other comprehensive income . . . . .	<u>853</u>	<u>963</u>	<u>678</u>

The accumulated benefit obligation for all defined benefit pension plans was US\$2,098 thousand, US\$2,648 thousand and US\$ 3,210 thousand at December 31, 2015, 2016 and 2017, respectively.

The components of net periodic benefit cost are as follows:

	<u>Year Ended December 31</u>		
	<u>2015</u>	<u>2016</u>	<u>2017</u>
	US\$	US\$	US\$
Service cost .....	273	487	1,572
Interest cost .....	57	104	336
Projected return on plan assets .....	(47)	(28)	(58)
Amortization of unrecognized net transition obligation and unrecognized net actuarial gain .....	<u>27</u>	<u>11</u>	<u>37</u>
Net periodic benefit cost .....	<u>310</u>	<u>574</u>	<u>1,887</u>

Other changes in plan assets and benefit obligation recognized in other comprehensive loss:

	<u>2015</u>	<u>2016</u>	<u>2017</u>
	US\$	US\$	US\$
	Recognize the decrease in net gain (loss) .....	4	111
Amortization of net gain (loss) .....	<u>—</u>	<u>(1)</u>	<u>—</u>
Total recognized in other comprehensive loss (income) .....	<u>4</u>	<u>110</u>	<u>(285)</u>

The estimated net gain for the defined benefit pension plans that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year is US\$33 thousand.

Expected benefit payments:

	US\$
2018 .....	188
2019 .....	184
2020 .....	407
2021 .....	181
2022 .....	182
2023 and thereafter .....	2,057

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

	<u>2015</u>		<u>2016</u>		<u>2017</u>	
	<u>Taiwan</u>	<u>Korea</u>	<u>Taiwan</u>	<u>Korea</u>	<u>Taiwan</u>	<u>Korea</u>
Weighted-average assumptions used to determine benefit obligations:						
Discount rate .....	1.75%	3.90%	1.50%	3.80%	1.63%	4.10%
Rate of compensation increase .....	4.25%	4.00%	4.25%	3.50%	4.25%	3.50%
Weighted-average assumptions used to determine net projected benefit cost:						
Discount rate .....	1.75%	3.90%	1.50%	3.80%	1.63%	4.10%
Expected long-term return on plan assets .....	2.00%	1.20%	2.00%	1.10%	1.75%	1.10%
Rate of compensation increase .....	4.25%	4.00%	4.25%	3.50%	4.25%	3.50%

In 2016 and 2017, FCI's pension plan assets were invested in principal guaranteed interest insurance contracts and fixed bank deposits, which are principal and interest guaranteed products and are classified as Level 2. These Level 2 securities were valued by discounting future cash flows using benchmark yield rates.

The fair values of FCI's pension plan assets at December 31, 2016 and 2017 are as follows:

	<b>December 31</b>	
	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>
Guaranteed interest contract		
Kyobo Life Insurance Co. Ltd. ....	1,284	1,599
Shinhan Investment Co. ....	—	374
Fixed deposit		
Industrial Bank of Korea ....	1,537	1,892
	<u>2,821</u>	<u>3,865</u>

## 15. INCOME TAXES

The components of income tax expense are as follows:

	<b>Year Ended December 31</b>		
	<b>2015</b>	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>	<b>US\$</b>
Current .....	17,338	31,063	23,465
Deferred .....	911	(3,373)	581
Income tax expense .....	<u>18,249</u>	<u>27,690</u>	<u>24,046</u>

The income (loss) before income taxes for domestic and foreign entities is as follows:

	<b>Year Ended December 31</b>		
	<b>2015</b>	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>	<b>US\$</b>
Domestic .....	(12,037)	(20,663)	(27,902)
Foreign .....	90,537	159,293	126,903
	<u>78,500</u>	<u>138,630</u>	<u>99,001</u>

Since the Company is based in the Cayman Islands, a British overseas territory with no corporate income tax, tax on pretax income is calculated at the Cayman Islands statutory rate of zero for each year.

The Company and its subsidiaries file separate income tax returns. A reconciliation of income tax expense on pretax income at statutory rate and income tax expense is shown below:

	<b>Year Ended December 31</b>		
	<b>2015</b>	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>	<b>US\$</b>
Tax expense at statutory rate of Cayman .....	—	—	—
Differences between Cayman and foreign statutory tax rates .....	18,765	34,415	24,255
Tax-exempt income .....	(906)	(4,648)	—
Permanent differences .....	(1,065)	(7,792)	(4,249)
Temporary differences .....	(330)	(1,533)	(1,445)
Alternative minimum tax .....	4	594	4
Income tax (10%) on undistributed earnings .....	2,460	5,677	2,709
Net changes in income tax credit .....	(897)	(495)	166
Net changes in valuation allowance of deferred income tax assets .....	1,621	1,724	(2,401)
Net operating loss carryforwards .....	(2,052)	(1,689)	1,492
Liabilities related to unrealized tax benefits .....	672	2,385	3,455
Adjustment of prior years' taxes and others .....	(23)	(948)	60
Income tax expense .....	<u>18,249</u>	<u>27,690</u>	<u>24,046</u>



Deferred income tax assets (liabilities) are as follows:

	<b>December 31</b>	
	<b>2016</b>	<b>2017</b>
	<b>US\$</b>	<b>US\$</b>
Notes and accounts receivable . . . . .	44	44
Stock-based compensation . . . . .	1,146	771
Allowance for sales return . . . . .	205	154
Inventory reserve . . . . .	1,646	1,311
Foreign currency translation . . . . .	2	( 5)
Property and equipment . . . . .	383	168
Investment tax credits . . . . .	8,647	9,078
Net operating loss carryforwards . . . . .	12,335	10,391
Others . . . . .	411	562
Valuation allowance . . . . .	<u>(20,836)</u>	<u>(19,072)</u>
	<u>3,983</u>	<u>3,402</u>

The valuation allowance shown in the table above relates to net operating loss carryforwards, tax credits and temporary differences for which the Company believes that realization is uncertain. Valuation allowance increased by US\$2,253 thousand and US\$1,792 thousand for the years ended December 31, 2015 and 2016, respectively, and decreased by US\$1,764 thousand for the year ended December 31, 2017. The increase in valuation allowance in 2015, and 2016 was primarily due to uncertainty in generating sufficient taxable income in the foreseeable future and utilizing operating loss carryforwards and research and development credits before they expire. The decrease in valuation allowance in 2017 was primarily due to the lower Federal corporate income tax rate that followed the enactment of the Tax Cuts and Jobs Act of 2017.

Starting from 2018, the corporate income tax rate in Taiwan increased from 17% to 20%. In addition, the rate of the corporate surtax applicable to 2018 unappropriated earnings was reduced from 10% to 5%. Deferred tax assets recognized as at December 31, 2017 are expected to be adjusted and would increase by US\$529 thousand in 2018.

As of December 31, 2017, FCI had unused research and development tax credits of approximately US\$4,546 thousand which will expire in the period from 2018 to 2022.

As of December 31, 2017, the Company’s United States federal net operating loss carryforwards for federal income tax purposes were approximately US\$9,760 thousand. If not utilized, the federal net operating loss carryforwards will expire in 2037.

As of December 31, 2017, the Company’s United States federal and state research and development tax credit carryforwards for federal and state income tax purposes were approximately US\$2,601 thousand and US\$1,785 thousand, respectively. If not utilized, the federal tax credit carryforwards will expire starting in 2037 while the state tax credit carryforward has no expiration date.

Current United States federal and California state laws include substantial restrictions on the utilization of net operating losses and credits in the event of an “ownership change” of a corporation. Accordingly, the Company’s ability to utilize net operating loss and tax credit carryforwards may be limited as a result of such “ownership change”. Such a limitation could result in the expiration of carryforwards before they are utilized.

As of December 31, 2017, the Company had accumulated undistributed earnings from a foreign subsidiary of US\$325 million. No deferred tax liability was recorded in respect of those amounts as these earnings are considered indefinitely reinvested. It is not practicable to estimate the amount of unrecognized deferred tax liabilities for these undistributed foreign earnings.

## Unrecognized Tax Benefit

A reconciliation of the beginning and ending balances of the total amounts of unrecognized tax benefits is as follows:

	Year Ended December 31		
	2015	2016	2017
	US\$	US\$	US\$
Balance, beginning of year	4,655	5,639	10,286
Increases in tax positions taken in current year	2,337	4,675	6,647
Decrease in tax position taken in prior year primarily related to the resolution of tax audit	(1,353)	(28)	(1,877)
Balance, end of year	<u>5,639</u>	<u>10,286</u>	<u>15,056</u>

At December 31, 2017, the Company had US\$15,056 thousand of unrecognized tax benefits that if recognized would affect the effective tax rate. For the years ended December 31, 2015, 2016 and 2017, the total amount of interest expense and penalties related to uncertain tax positions recorded in the provision for income tax expense was approximately US\$363 thousand, US\$575 thousand and US\$617 thousand, respectively. The total amount of accrued interest and penalties recognized as of December 31, 2016 and 2017 was US\$2,587 thousand and US\$3,421 thousand, respectively. The Company does not expect uncertain tax positions to change in the next twelve months, except in the case of settlements with tax authorities, the likelihood and timing of which are difficult to estimate.

The Company files income tax returns in United States and foreign jurisdictions. The following table summarizes the Company's major jurisdictions and tax year that remain subject to examination by tax authorities as of December 31, 2017:

<u>Tax Jurisdiction</u>	<u>Tax Years</u>
China	2014 and onward
Hong Kong	2014 and onward
Taiwan	2012 and onward
Korea	2012 and onward
United States	2012 onward

## 16. SHAREHOLDERS' EQUITY

### *Appropriations from Earnings*

In accordance with the amendments to the Company Act of the ROC in May 2015, the recipients of dividends and bonuses are limited to shareholders and do not include employees. The board of directors of SMI Taiwan held their meeting on June 29, 2016 and, in that meeting, had resolved amendments to the Company's Articles of Incorporation of SMI Taiwan, particularly the amendment to the policy on dividend distribution and the addition of the policy on distribution of employees' compensation.

Under the dividend policy of SMI Taiwan as set forth in the amended Articles, SMI Taiwan, the Company's largest subsidiary, must make appropriations from annual earnings to non-distributable reserve which could affect the Company's ability to pay cash or stock dividends, if any. SMI Taiwan subsidiary may only distribute dividends after it has made allowances as determined under ROC GAAP at each year-end for:

- Payment of taxes;
- Recovery of prior years' deficits, if any;
- 10% of remaining balance after deduction for a and b as legal reserve;

- d. Special reserve based on relevant laws or regulations or 10% of remaining balance for deduction from above a to c as special reserve when necessary.

## Dividends

The Company declared cash dividends per ordinary share during the periods presented as follows:

	2016		2017	
	Dividends Per Share (US\$)	Amount (in US\$ thousands)	Dividends Per Share (US\$)	Amount (in US\$ thousands)
First quarter	\$0.0375	\$ 5,290	\$0.050	\$ 7,134
Second quarter	\$0.0375	5,290	\$0.050	7,148
Third quarter	\$0.0375	5,297	\$0.050	7,155
Fourth quarter	\$0.0500	7,065	\$0.075	10,737
		<u>\$22,942</u>		<u>\$32,174</u>

On October 24, 2016 and October 24, 2017, our Board of Directors, instead of declaring a quarterly dividend, declared an annual dividend of US\$0.8 and US\$1.2 per ADS, equivalent to US\$0.2 and US\$0.3 per ordinary share, which will be paid in four quarterly installments starting in the fourth quarter of 2016 and 2017, respectively. Future dividends, if any, on the Company's outstanding ADSs and ordinary shares will be declared by and subject to the discretion of the Company's board of directors. If the Company's board of directors decides to distribute dividends, the form, frequency and amount of such dividends will depend upon the Company's future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors our board of directors may deem relevant.

Any future dividend the Company declares will be paid to the holders of ADSs, subject to the terms of the deposit agreement, to the same extent as holders of the Company's ordinary shares, to the extent permitted by applicable laws and regulations, less the fees and expenses payable under the deposit agreement. Any dividend the Company declares will be distributed by the depositary bank to the holders of our ADSs. Cash dividends on our ordinary shares, if any, will be paid in U.S. dollars.

## 17. EQUITY INCENTIVE PLAN

### *2005 Equity Incentive Plan and 2015 Equity Incentive Plan*

On April 22, 2005, the Company adopted its 2005 Equity Incentive Plan ("the 2005 Plan"). The 2005 Plan provides for the grant of stock options, stock bonuses, restricted stock awards, restricted stock units and stock appreciation rights, which may be granted to employees (including officers), directors and consultants. The 2005 Plan reserved 10,000 thousand shares of ordinary shares, inclusive of the number of assumed share options under the 2004 Plan, for issuance upon the exercise of stock options.

In 2006, the Company amended the 2005 Plan to reserve an additional 15,000 thousand ordinary shares for issuance upon exercise of stock options and restricted stock units. In 2009, the Company amended the Plan to reserve an additional 15,000 thousand ordinary shares for issuance upon exercise of stock options and restricted stock units.

Restricted stock units are converted into shares of the Company's ordinary shares upon vesting on one-for-one basis. The vesting of restricted stock unit is subject to the employee's continuing service to the Company. The cost of these awards is determined using the fair value of the Company's ordinary share on the date of the grant, and compensation is recognized on a straight-line basis over the requisite service period. The Company's restricted stock units are considered non-vested share awards as defined under ASC 718.

In April 2010, the Company's Board of Directors and Compensation Committee approved an employee stock option exchange program that required certain employees to exchange eligible stock options for a lesser number of new stock options that have approximately the same fair values as the options surrendered. Eligible options included stock options granted between August 17, 2005 and July 31, 2008 that had an exercised price above US\$1.85. In 2010, 4,369 thousand eligible stock options were exchanged for 3,785 thousand new stock options granted. The new stock options have an exercise price of US\$1.47, which was equal to the market price of the Company's ordinary share on April 26, 2010, the date eligible stock options were surrendered and new stock options granted. The new stock options were issued under the 2005 Plan and are subject to its terms and conditions. The new stock options will continue to vest according to the original vesting schedule. Using the Black-Scholes option pricing model, the Company determined that the fair value of the surrendered stock options on a grant-by-grant basis was approximately equal, as of the date of the exchange, to the fair value of the new stock options granted, resulting in insignificant incremental share-based compensation.

On June 3, 2015, the Company adopted its 2015 Equity Incentive Plan ("the 2015 Plan"). The 2015 Plan provides for the grant of stock options, stock bonuses, restricted stock awards, restricted stock units and stock appreciation rights, which may be granted to employees (including officers), directors and consultants. The 2015 Plan reserved 20,000 thousand shares of ordinary shares for issuance upon exercise of stock options and restricted stock units.

### Stock Option and Restricted Stock Units Activity

The following is a summary of, the 2005 Plan and the 2015 Plan, which includes stock options and restricted stock units:

	<u>Unit</u> <u>(in Thousands)</u>
Available for grant at January 1, 2015 . . . . .	1,687
Authorized . . . . .	20,000
Restricted stock units granted . . . . .	(2,000)
Option and restricted stock units forfeited . . . . .	<u>175</u>
Available for grant at December 31, 2015 . . . . .	19,862
Restricted stock units granted . . . . .	(1,446)
Option and restricted stock units forfeited . . . . .	<u>335</u>
Available for grant at December 31, 2016 . . . . .	18,751
Restricted stock units granted . . . . .	(1,391)
Option and restricted stock units forfeited . . . . .	<u>27</u>
Available for grant at December 31, 2017 . . . . .	<u><u>17,387</u></u>

## Stock Options

A summary of the stock option activity and related information is as follows:

	Number of Options Shares (in Thousands)	Weighted Average Exercise Price (US\$)	Weighted Average Remaining Contractual Life (Years)
Outstanding at January 1, 2015 .....	1,058	1.47	
Options forfeited .....	(143)	1.47	
Options exercised .....	(336)	1.47	
Outstanding at December 31, 2015 .....	<u>579</u>	<u>1.47</u>	0.92
Options vested and expected to vest after December 31, 2015 .....	579	1.47	0.92
Options forfeited .....	(257)	1.47	
Options exercised .....	(64)	1.47	
Outstanding at December 31, 2016 .....	<u>258</u>	<u>1.47</u>	0.25
Options vested and expected to vest after December 31, 2016 .....	258	1.47	0.25
Options exercised .....	(258)	1.47	
Outstanding at December 31, 2017 .....	<u>—</u>	<u>—</u>	—

No stock options were granted in 2015, 2016 and 2017. The intrinsic value of options exercised, determined as of the date of option exercise, was US\$3,688 thousand, US\$580 thousand and US\$3,040 thousand in 2015, 2016 and 2017, respectively.

As of December 31, 2017, total unrecognized compensation cost related to non-vested share-based compensation awards granted under the Company's stock option plans, net of estimated forfeitures, was nil.

The aggregate intrinsic value represents the total intrinsic value (the difference between the Company's closing stock price on the last trading day of fiscal year 2017 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on December 31, 2017. Intrinsic value will change in future periods based on the fair market value of the Company's stock and the number of shares outstanding.

The total cash received from employees as a result of employee stock option exercises were US\$494 thousand, US\$93 thousand and US\$380 thousand for the years ended December 31, 2015, 2016 and 2017, respectively.

The related tax effect for stock-based compensation benefit were US\$561 thousand, US\$37 thousand, and US\$124 thousand for 2015, 2016 and 2017, respectively. The related tax effect for stock-based compensation expense for option and restricted stock units exercised during 2015, 2016 and 2017 was US\$1,647 thousand, US\$1,702 thousand and US\$2,273 thousand, respectively. The related tax effect was determined using the applicable tax rates in jurisdictions to which this expense relates.

## Restricted Stock Units

A summary of the status of restricted stock units and changes is as follows:

	Number of Non-vested Stock Units (in Thousands)	Weighted Average Grant Date Fair Value (US\$)	Weight Average Remaining Recognition Period (Years)
Non-vested at January 1, 2015 .....	2,160	4.90	0.31
Restricted stock units granted .....	2,000	6.83	
Restricted stock units vested .....	(2,003)	4.96	
Restricted stock units forfeited .....	(32)	5.85	
Non-vested at December 31, 2015 .....	2,125	6.65	0.73
Restricted stock units granted .....	1,446	12.67	
Restricted stock units vested .....	(1,726)	6.46	
Restricted stock units forfeited .....	(78)	6.57	
Non-vested at December 31, 2016 .....	1,767	11.65	0.47
Restricted stock units granted .....	1,391	10.75	
Restricted stock units vested .....	(1,593)	12.08	
Restricted stock units forfeited .....	(27)	10.69	
Non-vested at December 31, 2017 .....	<u>1,538</u>	<u>10.36</u>	0.33

As of December 31, 2017, there was US\$4,736 thousand of total unrecognized compensation cost related to restricted stock units granted under the 2005 Plan and the 2015 Plan.

## Stock-based Compensation Expense

The following table shows total stock-based compensation expense included in the Consolidated Statements of Income for the years ended December 31, 2015, 2016 and 2017.

	Year Ended December 31		
	2015 US\$	2016 US\$	2017 US\$
Cost of sales .....	261	400	293
Research and development .....	6,565	10,529	9,255
Sales and marketing .....	1,790	3,122	3,167
General and administrative .....	1,802	3,313	2,779
	<u>10,418</u>	<u>17,364</u>	<u>15,494</u>

## 18. COMMITMENTS AND CONTINGENCIES

FCI provided their employees with collateral for personal loans which is deposited at a designated bank and the amount deposited was US\$415 thousand and US\$468 thousand at December 31, 2016 and 2017, respectively. Such amounts were accounted for as restricted cash.

## Operating Leases

The Company entered into various operating lease agreements for office space that expire on various dates through March 2022. The Company recognized rent expense for the years ended December 31, 2015, 2016 and 2017 of US\$2,453 thousand, US\$2,595 thousand and US\$3,131 thousand, respectively. The minimum operating lease payments expected under these leases as of December 31, 2017 were US\$3,711 thousand, US\$3,070 thousand, US\$1,541 thousand, US\$1,159 thousand, and US\$65 thousand for the years ending December 31, 2018, 2019, 2020, 2021 and 2022, respectively.



## Litigation

The Company is subject to legal proceedings and claims, either asserted or unasserted, which arise in the ordinary course of business. Although the outcome of such proceedings and claims cannot be predicted with certainty, management does not believe that the outcome of any of these matters will have a material adverse effect on our business, results of operations, financial position or cash flows. Any litigation, however, involves potential risk and potentially significant litigation costs, and therefore there can be no assurance that any litigation which is now pending or which may arise in the future would not have such a material adverse effect on our business, financial position, results of operations or cash flows.

All American Semiconductor, Inc. (“All American” or “AASI”) was a former distributor for the Company. On April 25, 2007, All American filed for Chapter 11 bankruptcy protection. At the time of the filing, the Company had US\$256 thousand of unpaid accounts receivable from All American. On April 17, 2009 SMI USA and related entities were named as defendants in an adversary proceeding filed by the AASI Creditor Liquidating Trust (“CLT”) in the bankruptcy case pending in the U.S. Bankruptcy Court for the Southern District of Florida. The CLT was seeking the return of allegedly avoidable transfers in the amount of US\$854 thousand. SMI USA filed an answer and affirmative defenses. In March 2010, SMI USA settled with the CLT by paying the amount of US\$220 thousand and on April 1, 2010, the Bankruptcy Court granted the motion to approve stipulations to compromise controversy. On August 23, 2010, the Court entered an order dismissing the adversary proceeding. In June 2011, Liquidating Trustee for the CLT filed the AASI Creditor Liquidating Trustee’s Seventeenth Omnibus Objection to Claims but in August 2011, withdrew it with respect to SMI USA’s proof of claim. As a holder of allowed claims, we are entitled to receive distribution pursuant to the bankruptcy plan. On December 31, 2017, we received total distributions of US\$265 thousand from the CLT. We are not expecting further distributions.

## 19. SEGMENT INFORMATION

The Company is the global leader and pioneer in developing NAND flash controllers for solid storage devices. The Company currently operates as one reportable segment. The chief operating decision maker is the Chief Executive Officer.

The Company groups its products into three categories, based on the markets in which they may be used. The following summarizes the Company’s revenue by product category:

	Year Ended December 31		
	2015	2016	2017
	US\$	US\$	US\$
Mobile Storage . . . . .	302,910	510,687	480,735
Mobile Communications . . . . .	50,896	39,322	37,447
Others . . . . .	7,491	6,137	5,222
	<u>361,297</u>	<u>556,146</u>	<u>523,404</u>

Revenue is attributed to a geographic area based on the bill-to location. The following summarizes the Company’s revenue by geographic area:

	Year Ended December 31		
	2015	2016	2017
	US\$	US\$	US\$
Taiwan . . . . .	71,387	75,926	72,768
United States . . . . .	39,558	59,390	40,344
Japan . . . . .	19,636	17,070	18,797
Korea . . . . .	150,118	183,249	176,813
China . . . . .	69,623	151,112	126,048
Others . . . . .	10,975	69,399	88,634
	<u>361,297</u>	<u>556,146</u>	<u>523,404</u>

Major customers representing at least 10% of net sales

	Year Ended December 31					
	2015		2016		2017	
	US\$	%	US\$	%	US\$	%
SK Hynix .....	108,645	30	156,541	28	150,762	29
Intel .....	*	*	*	*	50,205	10

\* Less than 10%

Long-lived assets (property and equipment, net) by geographic area were as follows:

	Year Ended December 31		
	2015	2016	2017
	US\$	US\$	US\$
Taiwan .....	32,014	34,011	36,369
United States .....	274	237	242
Korea .....	1,891	1,448	1,936
China .....	16,268	12,181	12,798
Japan .....	22	15	25
	<u>50,469</u>	<u>47,892</u>	<u>51,370</u>

## 20. FAIR VALUE MEASUREMENT

The following section describes the valuation methodologies the Company uses to measure assets and liabilities at fair value.

The Company uses quoted prices in active markets for identical assets to determine fair value where applicable. This pricing methodology applies to Level 1 investments such as bond funds. The fair value of the principal protected notes was determined by its present value utilizing rate of return as the market observable input and therefore, these are classified as Level 2 instruments. This is because there generally are no quoted prices in active markets for identical principal protected notes at the reporting date. Hence, in order to determine the fair value, the Company must use observable inputs other than quoted prices in active markets for identical or similar instruments, quoted prices for similar instruments in active markets, or other inputs that are observable.

For the years ended December 31, 2016 and 2017, none of the Company's assets measured on a recurring basis was determined by using significant unobservable inputs.

The following table presents our assets measured at fair value on a recurring basis as of December 31, 2016 and 2017:

December 31, 2016

	Level 1	Level 2	Level 3	Total
	US\$	US\$	US\$	US\$
Assets				
Short-term investments — trading securities .....	695	2,607	—	3,302

December 31, 2017

	Level 1	Level 2	Level 3	Total
	US\$	US\$	US\$	US\$
Assets				
Short-term investments — trading securities .....	755	6,186	—	6,941

**Subsidiaries of Silicon Motion Technology Corporation**

<u>Name of Entity</u>	<u>Jurisdiction of Incorporation</u>
FCI Inc.	Korea
Silicon Motion K.K.	Japan
Silicon Motion Korea Ltd.	Korea
Silicon Motion Technology (HK) Ltd	Hong Kong
Silicon Motion, Inc.	California
Silicon Motion, Inc.	Taiwan
Silicon Motion, Inc. (Beijing)	China
Silicon Motion, Inc. (Shanghai)	China
Silicon Motion, Inc. (Shenzhen)	China
Shannon Systems	China
Bigtera Limited	Hong Kong

**Certification by the Chief Executive Officer Pursuant to  
Section 302 of the Sarbanes-Oxley Act of 2002**

I, Wallace C. Kou, certify that:

1. I have reviewed this annual report on Form 20-F of Silicon Motion Technology Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - (c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of company's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: April 30, 2018

/s/ Wallace C. Kou

Name: Wallace C. Kou

Title: Chief Executive Officer

**Certification by the Chief Financial Officer Pursuant to  
Section 302 of the Sarbanes-Oxley Act of 2002**

I, Riyadh Lai, certify that:

1. I have reviewed this annual report on Form 20-F of Silicon Motion Technology Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - (c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of company's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Date: April 30, 2018

/s/ Riyadh Lai

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Name: Riyadh Lai

Title: Chief Financial Officer

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned each hereby certifies that, to his knowledge, the annual report on Form 20-F of Silicon Motion Technology Corporation for the year ended December 31, 2017 fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, and that the information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of Silicon Motion Technology Corporation.

The foregoing certification is being furnished pursuant to 18 U.S.C. Section 1350 solely for purposes of complying with the provisions of Section 906 of the Sarbanes-Oxley Act of 2002, is not intended to be used or relied upon for any other purpose and is not being filed as part of the periodic report or as a separate disclosure document.

Date: April 30, 2018

/s/ Wallace C. Kou

Name: Wallace C. Kou

Title: Chief Executive Officer

/s/ Riyadh Lai

Name: Riyadh Lai

Title: Chief Financial Officer



**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in Registration Statement Nos. 333-161599, 333-142422, 333-131219 and 333-204876 on Forms S-8 of our reports dated April 30, 2018, relating to the consolidated financial statements of Silicon Motion Technology Corporation and subsidiaries (which report expresses an unqualified opinion) and the effectiveness of Silicon Motion Technology Corporation and subsidiaries' internal control over financial reporting, appearing in the Annual Report on Form 20-F of Silicon Motion Technology Corporation for the year ended December 31, 2017.

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

April 30, 2018

## Board of Directors

- **James Chow**  
*Chairman of the Board*  
Silicon Motion Technology Corporation
- **Wallace C. Kou**  
*President & Chief Executive Officer*  
Silicon Motion Technology Corporation
- **Steve Chen**  
*Chairman*  
Mercuries Co., Ltd.
- **Tsung-Ming Chung**  
*Chairman*  
Dynapack International Technology Corp.
- **Lien-Chun Liu**  
*Vice President*  
International Council of Women
- **Yung-Chien Wang**  
*Vice President*  
Professional Trust Co., Ltd.
- **Han-Ping D. Shieh**  
*Chair Professor*  
National Chiao Tung University

## ADS Listing

Our American Depositary Shares (ADSs) trade on the NASDAQ Global Select Market under the symbol "SIMO"

## ADS Depository

The Bank of New York Mellon, New York, NY

## Legal Counsel

K&L Gates, Taipei, Taiwan

## Independent Auditors

Deloitte & Touche, Taipei, Taiwan

## Executive Officers

- **Wallace C. Kou**  
*President & Chief Executive Officer*
- **Riyadh Lai**  
*Chief Financial Officer*
- **Nelson Duann**  
*Senior VP of Marketing & OEM Business, Mobile Storage*
- **Sangwoo Han**  
*Senior VP and General Manager, Mobile Communications*
- **Xueshi Yang**  
*Senior VP and General Manager, Shannon Systems*
- **Arthur Yeh**  
*VP of Sales, Mobile Storage*
- **Robert Fan**  
*President of SMI USA*
- **John (Chun-O) Kim**  
*VP of Sales, Mobile Communications*
- **David Yu**  
*VP of Sales & Marketing, Shannon Systems*
- **Leander Yu**  
*VP of Sales & Marketing, Bigtera*
- **Frank Chang**  
*VP of R&D, Mobile Storage*
- **Ken Chen**  
*VP of Operations*
- **Kevin Yeh**  
*VP of R&D, Algorithm & Technology*
- **John (Jong Ryul) Lee**  
*VP of R&D, Mobile Communications*
- **Derek Zhou**  
*VP of R&D, Shannon Systems*
- **Jason Chiang**  
*VP of HR and Administration and Special Assistant to CEO*
- **Frank Shu**  
*VP of R&D, Verification Engineering & Compatibility Test*
- **Mike Jing**  
*VP of IT*

## Investor Relations

For more information about Silicon Motion, please visit our website at [www.siliconmotion.com](http://www.siliconmotion.com) or e-mail us at [ir@siliconmotion.com](mailto:ir@siliconmotion.com)

