6. Financial Highlights

6.1 Financial Status and Operating Results

6.1.1 Financial Status

Consolidated

Unit: NT$ thousands

Item	2013	2012	Difference	%
Current Assets	358,486,654	250,325,436	108,161,218	43%
Long-term Investments (Note 1)	89,183,810	65,717,240	23,466,570	36%
Property, Plant and Equipment	792,665,913	617,562,188	175,103,725	28%
Intangible Assets	11,490,383	10,959,569	530,814	5%
Other Assets (Note 2)	11,228,217	16,790,075	(5,561,858)	-33%
Total Assets	1,263,054,977	961,354,508	301,700,469	31%
Current Liabilities	189,777,934	148,473,947	41,303,987	28%
Noncurrent Liabilities	225,501,958	89,786,655	135,715,303	151%
Total Liabilities	415,279,892	238,260,602	177,019,290	74%
Capital Stock	259,286,171	259,244,357	41,814	0%
Capital Surplus	55,858,626	55,675,340	183,286	0%
Retained Earnings	518,193,152	408,411,468	109,781,684	27%
Equity Attributable to Shareholders of the Parent	847,508,255	720,550,680	126,957,575	18%
Total Equity	847,775,085	723,093,906	124,681,179	17%

Note 1: Long-term investments consist of noncurrent available-for-sale financial assets, financial assets carried at cost and investments accounted for using equity method.
Note 2: Other assets consist of deferred income tax assets, refundable deposits, and other noncurrent assets.

- **Analysis of Deviation over 20%**

The increase in current assets was mainly due to increase in cash and cash equivalents in 2013.
The increase in long-term investments was mainly due to increase in fair value of available-for-sale financial assets in 2013.
The increase in property, plant and equipment was mainly due to acquisition of advanced technology equipment during 2013.
The decrease in other assets was mainly due to decrease in deferred income tax assets.
The increase in total assets was mainly due to increase in cash and cash equivalents and property, plant and equipment.
The increase in current liabilities was mainly due to increase in payables to contractors and equipment suppliers and income tax payable, partially offset by decrease in short-term loans.
The increase in noncurrent liabilities was mainly due to issuance of corporate bonds of NT$130.8 billion in 2013.
The increase in total liabilities was mainly due to increase in noncurrent liabilities.
The increase in retained earnings was mainly due to net income of 2013, partially offset by distribution of 2012 earnings.

- **Major Impact on Financial Position**

The above deviations had no major impact on TSMC's financial position.

- **Future Plan on Financial Position**: Not applicable.

In 2013, net income registered a record level of NT$188.1 billion with EPS of NT$7.26.

Unconsolidated

Unit: NT$ thousands

Item	2013	2012	Difference	%
Current Assets	257,623,763	205,819,614	51,804,149	25%
Long-term Investments (Note 1)	165,545,159	139,634,200	25,910,959	19%
Property, Plant and Equipment	770,443,494	586,636,036	183,807,458	31%
Intangible Assets	7,069,456	6,449,837	619,619	10%
Other Assets (Note 2)	7,897,131	13,597,966	(5,700,835)	-42%
Total Assets	1,208,579,003	952,137,653	256,441,350	27%
Current Liabilities	187,195,744	144,528,616	42,667,128	30%
Noncurrent Liabilities	173,875,004	87,058,357	86,816,647	100%
Total Liabilities	361,070,748	231,586,973	129,483,775	56%
Capital Stock	259,286,171	259,244,357	41,814	0%
Capital Surplus	55,858,626	55,675,340	183,286	0%
Retained Earnings	518,193,152	408,411,468	109,781,684	27%
Total Equity	847,508,255	720,550,680	126,957,575	18%

Note 1: Long-term investments consist of financial assets carried at cost and investments accounted for using equity method.
Note 2: Other assets consist of deferred income tax assets, refundable deposits, and other noncurrent assets

- Analysis of Deviation over 20%

The increase in current assets was mainly due to increase in cash and cash equivalents in 2013.
The increase in property, plant and equipment was mainly due to acquisition of advanced technology equipment during 2013.
The decrease in other assets was mainly due to decrease in deferred income tax assets.
The increase in total assets was mainly due to increase in cash and cash equivalents and property, plant and equipment.
The increase in current liabilities was mainly due to increase in payables to contractors and equipment suppliers and income tax payable, partially offset by decrease in short-term loans.
The increase in noncurrent liabilities was mainly due to issuance of corporate bonds of NT$86.2 billion in 2013.
The increase in total liabilities was mainly due to increase in noncurrent liabilities.
The increase in retained earnings was mainly due to net income of 2013, partially offset by distribution of 2012 earnings.

- Major Impact on Financial Position

The above deviations had no major impact on TSMC's financial position.

- **Future Plan on Financial Position:** Not applicable.

6.1.2 Financial Performance

Consolidated

Unit: NT$ thousands

Item	2013	2012	Difference	%
Net Revenue	597,024,197	506,745,234	90,278,963	18%
Cost of Revenue	316,057,820	262,583,098	53,474,722	20%
Gross Profit before Unrealized Gross Profit on Sales to Associates	280,966,377	244,162,136	36,804,241	15%
Unrealized Gross Profit on Sales to Associates	(20,870)	(25,029)	4,159	-17%
Gross Profit	280,945,507	244,137,107	36,808,400	15%
Operating Expenses	71,563,234	62,510,875	9,052,359	14%
Other Operating Income and Expenses, Net	47,090	(449,364)	496,454	NM (Note)
Income from Operations	209,429,363	181,176,868	28,252,495	16%
Non-operating Income and Gains	6,057,759	499,588	5,558,171	1113%
Income before Income Tax	215,487,122	181,676,456	33,810,666	19%
Income Tax Expenses	27,468,185	15,552,654	11,915,531	77%
Net Income	188,018,937	166,123,802	21,895,135	13%
Other Comprehensive Income, Net of Income Tax	16,352,248	4,252,632	12,099,616	285%
Total Comprehensive Income for the Year	204,371,185	170,376,434	33,994,751	20%
Total Net Income Attributable to Shareholders of the Parent	188,146,790	166,318,286	21,828,504	13%
Total Comprehensive Income Attributable to Shareholders of the Parent	204,505,782	170,521,543	33,984,239	20%

Note: NM stands for non-meaningful.

- Analysis of Deviation over 20%

Increase in cost of revenue: The increase was mainly due to higher sales.
Increase in other operating income and expenses, net: The increase was mainly due to impairment loss related to property, plant and equipment recognized in 2012.
Increase in non-operating income and gains: The increase was primarily due to increase in earnings of equity method investees, lower impairment loss of financial assets recognized in 2013, partially offset by higher interest expenses for corporate bonds in 2013.
Increase in income tax expenses: The increase was mainly due to higher taxable income, the AMT tax rate changed from 10% to 12% and increase in income tax on unappropriated earnings.
Increase in other comprehensive income, net of income tax: The increase was mainly due to exchange rate differences arising from translation of foreign operations and the increase in fair value of available-for-sale financial assets in 2013.
Increase in total comprehensive income and total comprehensive income attributable to shareholders of the parent: The increase was mainly due to higher net income and other comprehensive income in 2013.

- Sales Volume Forecast and Related Information

For additional details, please refer to "*1. Letter to Shareholders*" on pages 2-5 of this Annual Report.

- Major Impact on Financial Performance

The above deviations had no major impact on TSMC's financial performance.

- **Future Plan on Financial Performance:** Not applicable.

Unconsolidated

Unit: NT$ thousands

Item	2013	2012	Difference	%
Net Revenue	591,087,600	500,369,525	90,718,075	18%
Cost of Revenue	319,407,163	265,494,185	53,912,978	20%
Gross Profit before Unrealized Gross Profit on Sales to Subsidiaries and Associates	271,680,437	234,875,340	36,805,097	16%
Unrealized Gross Profit on Sales to Subsidiaries and Associates	(35,577)	(25,029)	(10,548)	42%
Gross Profit	271,644,860	234,850,311	36,794,549	16%
Operating Expenses	66,924,354	57,481,083	9,443,271	16%
Other Operating Income and Expenses, Net	(66,614)	(549,087)	482,473	-88%
Income from Operations	204,653,892	176,820,141	27,833,751	16%
Non-operating Income and Gains	11,062,658	6,932,246	4,130,412	60%
Income before Income Tax	215,716,550	183,752,387	31,964,163	17%
Income Tax Expenses	27,569,760	17,434,101	10,135,659	58%
Net Income	188,146,790	166,318,286	21,828,504	13%
Other Comprehensive Income, Net of Income Tax	16,358,992	4,203,257	12,155,735	289%
Total Comprehensive Income for the Year	204,505,782	170,521,543	33,984,239	20%

- Analysis of Deviation over 20%

Increase in cost of revenue: The increase was mainly due to higher sales.
Increase in unrealized gross profit on sales to subsidiaries and associates: The increase was mainly due to higher sales to subsidiaries and associates in the fourth quarter 2013.
Decrease in other operating income and expenses, net: The decrease was mainly due to property, plant and equipment impairment loss during 2012.
Increase in non-operating income and gains: The increase was primarily due to increase in earnings of equity method, less impairment loss of financial assets recognized in 2013, partially offset by higher interest expenses for corporate bonds in 2013.
Increase in income tax expenses: The increase was mainly due to higher taxable income, the AMT tax rate changed from 10% to 12% and income tax on unappropriated earnings.
Increase in other comprehensive income, net of income tax: The increase was mainly due to exchange rate differences arising from translation of foreign operations and the increase in other comprehensive income of subsidiaries and associates in 2013.
Increase in total comprehensive income: The increase was mainly due to higher net income and other comprehensive income in 2013.

• Sales Volume Forecast and Related Information

For additional details, please refer to "*1. Letter to Shareholders*" on pages 2-5 of this Annual Report.

• Major Impact on Financial Performance

The above deviations had no major impact on TSMC's financial performance.

• Future Plan on Financial Performance: Not applicable.

6.1.3 Cash Flow

Consolidated

Unit: NT$ thousands

Cash Balance 12/31/2012	Net Cash Provided by Operating Activities in 2013	Net Cash Used in Investing and Financing Activities in 2013	Cash Balance 12/31/2013	Remedy for Liquidity Shortfall	
				Investment Plan	Financing Plan
143,410,588	347,383,537	(248,098,678)	242,695,447	None	None

• Analysis of Cash Flow

NT$347.4 billion net cash generated by operating activities: mainly from net income and depreciation/amortization.

NT$281.1 billion net cash used in investing activities: primarily for capital expenditures.

NT$33 billion net cash generated by financing activities: mainly from issuance of corporate bonds, partially offset by payment of cash dividends and decrease in short-term loans.

• Remedial Actions for Liquidity Shortfall: As a result of positive operating cash flows and cash on-hand, remedial actions are not required.

• Cash Flow Projection for Next Year: Not applicable.

Unconsolidated

Unit: NT$ thousands

Cash Balance 12/31/2012	Net Cash Provided by Operating Activities in 2013	Net Cash Used in Investing and Financing Activities in 2013	Cash Balance 12/31/2013	Remedy for Liquidity Shortfall	
				Investment Plan	Financing Plan
109,150,810	335,283,326	(297,995,368)	146,438,768	None	None

• Analysis of Cash Flow

NT$335.3 billion net cash generated by operating activities: mainly from net income and depreciation/amortization.

NT$284.4 billion net cash used in investing activities: primarily for capital expenditures.

NT$13.6 billion net cash used in financing activities: mainly from payment of cash dividends and decrease in short-term loans, partially offset by issuance of corporate bonds.

• Remedial Actions for Liquidity Shortfall: As a result of positive operating cash flows and cash on-hand, remedial actions are not required.

• Cash Flow Projection for Next Year: Not applicable.

6.1.4 Major Capital Expenditures and Impact on Financial and Business

Unit: NT$ thousands

Plan	Actual or Planned Source of Capital	Total Amount as of 12/31/2013	Actual Use of Capital	
			2013	2012
Production Facilities, R&D and Production Equipment	Cash flow generated from operations and issuance of corporate bonds	527,715,597	283,822,265	243,893,332
Others	Cash flow generated from operations	6,016,537	3,772,508	2,244,029
Total		533,732,134	287,594,773	246,137,361

Based on capital expenditures listed above and projected for 2014, it is estimated that TSMC's annual production capacity will increase by approximately 1.64 million 8-inch equivalent wafers in 2014.

6.1.5 Long-term Investment Policy and Results

TSMC's long-term investments, accounted for under the equity method, were all made for strategic purposes. However, when an investment is no longer of strategic value, it may be considered a financial investment. In 2013, the investment gain from these investments amounted to NT$9,530,933 thousand (NT$3,972,031 thousand on a consolidated basis), increasing significantly compared to 2012 mainly due to the high growth of mobile computing products and the recovery of solar market. For future investments, TSMC will continue to focus on strategic purposes through prudent assessments.

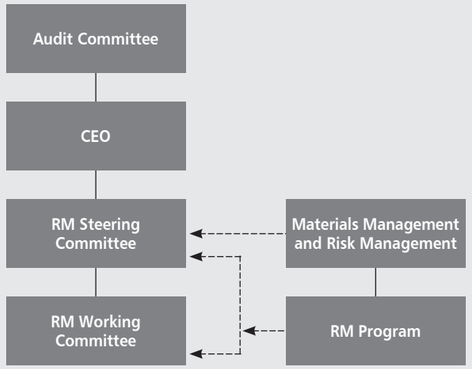
6.2 Risk Management

TSMC and its subsidiaries are committed to proactively and cost effectively integrating and managing strategic, operational, financial and hazardous risks together with potential consequences to operations and revenue. TSMC operates an Enterprise Risk Management (ERM) program based on both its corporate vision and its long-term sustainability and responsibility to both industry and society. ERM seeks to provide the appropriate management of risks by TSMC on behalf of all stakeholders. A Risk MAP that considers likelihood and impact severity is applied for identifying and prioritizing corporate risks. Various risk treatment strategies are also adopted in response to identified corporate risks.

To reduce TSMC's supply chain risks, a cross-function taskforce comprised of members from fab operations, material management, risk management and quality system management worked with TSMC's primary suppliers to develop business continuity plans, and enhance supply chain resilience capability through effectively manage the risks faced by its suppliers. As a result of those efforts, there was no interruption in TSMC's supply lines in 2013.

As TSMC continued to expand production capacity with advanced technology in 2013, seismic protection engineering design, risk treatment practices and green factory projects were initiated and implemented, beginning in the design phase for all new fabs.

6.2.1 Risk Management (RM) Organization Chart



• RM Steering Committee

Reports to Audit Committee;
Is composed of functional heads;
Reviews risk control progress; and
Identifies and approves the prioritized risk lists.

• RM Working Committee

Is composed of representatives from each function;
Periodically reviews risk control associated with business or manufacturing process changes;
Aligns functional ERM activities; and,
Follows up the risk control action plan

• RM Program

Coordinates the RM Working Committee activities;
Facilitates functional risk management activities;
Initiates cross function communication for risk mitigation; and,
Consolidates ERM reports into the RM Steering Committee

6.2.2 Strategic Risks

Risks Associated with Changes in Technology and Industry

• Industry Developments

The electronics industries and semiconductor market are cyclical and subject to significant, and often rapid, increases and decreases in product demand. TSMC's semiconductor foundry business is affected by the market conditions of the highly cyclical electronics and semiconductor industries in which most of its customers operate. Variations in order levels from customers result in volatility in the Company's revenues and earnings.

From time to time, the electronics and semiconductor industries have experienced significant, and sometimes prolonged, periods of downturns and overcapacity. Because TSMC is, and will continue to be, dependent on the requirements of electronics and semiconductor companies for its services, periods of downturn and overcapacity in the general electronics and semiconductor industries could lead to reduced demand for overall semiconductor foundry services, including TSMC's services. If TSMC cannot take appropriate actions such as reducing its costs to sufficiently offset declines in demand, the Company's revenues, margins and earnings will suffer during periods of downturn and overcapacity. Furthermore, due to the increasingly complex technological nature of our foundry services, the amount of our accounting provisions may also need to be provided and adjusted for potential sales returns and allowances to customers that may adversely affect the results of our operations.

- Changes in Technology

The semiconductor industry and its technologies are constantly changing. TSMC competes by developing process technologies using increasingly advanced nodes and with manufacturing products with more functions. TSMC also competes by developing new derivative technologies. If TSMC does not anticipate these changes in technologies or fails to rapidly develop new and innovative technologies, or if the Company's competitors unforeseeably gain sudden access to additional technologies, TSMC may not be able to provide foundry services on competitive terms. In addition, TSMC's customers have significantly decreased the time in which their products or services are launched into the market. If TSMC is unable to meet these shorter product times-to-market, TSMC risks losing these customers. These factors have also been intensified by the shift of the global technology market to consumer driven products such as mobile devices, and increasing concentration of customers and competition (all further discussed among these risk factors). These challenges also place greater demands on its research and development capabilities. If TSMC is unable to innovate new technologies that meet the demands of its customers or overcome the above factors, its revenues may decline significantly. Although TSMC has concentrated on maintaining a competitive edge in research and development, if TSMC fails to achieve advances in technologies or processes, or to obtain access to advanced technologies or processes developed by others, it may become less competitive.

Regarding the response measures for the above-mentioned risks, please refer to "*2.2.4 TSMC Position, Differentiation and Strategy*" on pages 10-11 of this Annual Report.

Risks Associated with Decrease in Demand and Average Selling Price

A vast majority of the Company's revenue is derived from customers who use TSMC's services in communication devices, personal computers, consumer electronics products and industrial/standard products. Any significant decrease in the demand for any one of these products may decrease the demand for such other products as well as overall global semiconductor foundry services, including TSMC's services, and may adversely affect the Company's revenues. Further, a significant portion of TSMC's operating costs is fixed because the Company owns most of its manufacturing capacities. In general, these costs do not decline when customer demand or TSMC's capacity utilization rates drop, and thus declines in customer demand, among other factors, may significantly decrease margins. Conversely, as product demand rises and factory utilization increases, the fixed costs are spread over increased output, which can improve TSMC's margins. Additionally, the historical and current trend of declining average selling prices of end-use applications places downward pressure on the prices of the components that go into such applications. If the average selling prices of end-use applications continue to decrease, the pricing pressure on components produced by the Company may lead to a reduction of TSMC's revenues, margin and earnings.

Risks Associated with Competition

The markets for our foundry services are highly competitive. We compete with other foundry service providers, as well as integrated device manufacturers that devote a significant portion of their manufacturing capacity to foundry operations. Some of these companies may have access to more advanced technologies and greater financial and other resources than TSMC, such as the possibility of receiving direct or indirect government bailout/economic stimulus funds or other incentives that are unavailable to us. The Company's competition may, from time to time, also decide to undertake aggressive pricing initiatives in one or more technology nodes. Increases in these competitive activities may decrease TSMC's customer base, TSMC's average selling prices, or both.

For example, over the past few years, TSMC has seen the rise of certain companies with the capability of providing foundry services. These companies are committed to trying to attract TSMC's customers. If TSMC is unable to compete with any and each of these new competitors with better technologies and manufacturing capacity and capabilities, it risks losing customers to these new contenders.

The Company competes primarily on the basis of process technology, manufacturing quality and service. The level of competition differs according to the process technology involved. For example, in more mature technologies, competitors tend to be more numerous and specialized. Some companies compete with TSMC in selected geographic regions or in application end markets. In recent years, substantial investments have been made by others to establish new pure-play foundry companies in mainland China and elsewhere, or to spin off the manufacturing operations of integrated device manufacturers (IDMs) and transform them into a pure-play foundry company.

Risks Associated with Changes in the Government Policies and Regulatory Environment

TSMC management closely monitors all domestic and foreign governmental policies and regulations that might impact TSMC's business and financial operations. As of February 28, 2014, the following changes or developments in governmental policies and regulations may influence the Company's business operations:

The Taiwan Financial Supervisory Commission (FSC) requires listed companies, starting from January 1, 2013, to prepare their consolidated financial statements in accordance with Taiwan's "Guidelines Governing the Preparation of Financial Reports by Securities Issuers" (the "Financial Reporting Guideline") and the following FSC endorsed standards and interpretations: "International Financial Reporting Standards," "International Accounting Standards," and relevant Interpretations (collectively, "Taiwan-IFRSs"). TSMC has already prepared its 2013 annual and interim consolidated financial statements in accordance with the Financial Reporting Guideline and Taiwan-IFRSs.

The Taiwan "National Health Insurance Act" was amended in January 2011, to create an obligation for employers and employees to pay an extra 2% "supplementary premium," effective from January 1, 2013. TSMC pays such extra 2% "supplementary premium" when TSMC distributes employees' profit sharing and variable bonus.

According to the "Income Basic Tax Act" (i.e., Alternative Minimum Tax, "AMT") amended in August, 2012, effective on January 1, 2013, the corporate income tax rate of AMT will be increased from 10% to 12%. TSMC has evaluated the impact of these amendments on its financial statements and implemented such amendments according to the relevant laws.

The "Labor Safety and Health Act" of Taiwan was amended and renamed as the "Occupational Safety and Health Act" in July, 2013. Highlights of the amendment include: expanding the applicability of the Act to employees of all occupations; building a comprehensive occupational disease prevention system; strengthening the protection of the mental and physical health of workers; stipulating maternity protection and employment equality; and requiring high-risk business to regularly implement safety assessments. TSMC over the years has been consistently maintaining a robust safe and healthy work environment and protective measures in place, and will continue to maintain the safety and health of its workplace in compliance with applicable laws and regulations. In addition, the Taiwan legislative authority has been studying relevant laws relating to environmental protection and employee safety and health protection (e.g. "Greenhouse Gas Reduction Act" and "Energy Tax Act"). Though the "Greenhouse Gas Reduction Act" has not been passed, TSMC has been implementing various long-term energy saving and carbon reduction programs since 2000. As to the proposed "Energy Tax Act," there has been no concrete guidance or law issuing from the Taiwan government as of yet, so the impacts of such law are indeterminable at the moment. However, it is very likely that such law may increase the operating costs of the Company.

Other than the above laws and regulations, it is not expected that other governmental policies or regulatory changes would materially impact TSMC's operations and financial condition.

6.2.3 Operational Risks

Risks Associated with Capacity Expansion

TSMC performs long-term market demand forecasts to estimate market and general economic conditions for its products and services. Based upon these estimates, TSMC manages its overall capacity in accordance with market demand. Because market conditions may vary significantly and unexpectedly, our market demand forecast may change significantly at any time. Further, since certain manufacturing lines or tools in some of TSMC's manufacturing facilities may be suspended or shut down temporarily during periods of decreased demand, the Company may not be able to ramp up in a timely manner during periods of increased demand. During periods of continued decline in demand, our operating facilities may not be able to absorb and complete in a timely manner outstanding orders re-directed from shuttered facilities.

Recently, TSMC has been adding capacity to its 12-inch wafer fabs in the Hsinchu Science Park, Southern Taiwan Science Park and Central Taiwan Science Park, based on our market demand forecasts taking into account the demand forecasts of our customers. As a result, the total monthly capacity of the Company's 12-inch wafer fabs was increased from 366,800 wafers as of December 31, 2012 to 414,700 wafers as of December 31, 2013. Expansion and modification of the Company's production facilities will, among other factors, increase TSMC's costs. For example, the Company will need to purchase additional equipment, train personnel to operate the new equipment, or hire additional personnel. If TSMC cannot increase its net revenue accordingly, in order to offset these higher costs, TSMC's financial performance may be adversely affected.

TSMC has established systems and processes to evaluate and forecast market demand and refers to these forecasts and evaluations when considering whether to expand or reduce capacity. As of the date of this Annual Report, the benefits brought about by such capacity expansion were in line with TSMC's expectations.

Risks Associated with Sales Concentration

Over the years, TSMC's customer profile and the nature of its customers' business have changed dramatically. While it generates revenue from hundreds of customers worldwide, TSMC's ten largest customers accounted for approximately 60% and 62% of net revenue in 2012 and 2013, respectively, and the Company's largest customer accounted for approximately 17% and 22% of net revenue in 2012 and 2013, respectively.

This customer concentration results in part from the changing dynamics of the electronics industry with the structural shift to mobile devices and applications and software that provide the content for such devices. There are only a limited number of customers who are successfully exploiting this new business model paradigm.

Also, in order to respond to the new business model paradigm, TSMC has seen the nature of its customers' business models change. For example, there is a growing trend toward the rise of system houses that operate in a manner that makes their products and services more marketable to the changing consumer market. The loss of, or significant curtailment of, purchases by one or more of the Company's top customers, including curtailment due to increased competitive pressures, industrial consolidation, a change in their designs, or change in their manufacturing sourcing policies, or practices of these customers, or the timing of customer or distributor inventory adjustments, or change in its major customers' business models may adversely affect TSMC's results of operations and financial condition.

We will keep a close watch on these trends and work closely with our customers to respond to these changes and to strengthen our market position.

Risks Associated with Purchase Concentration

- Raw Materials

TSMC's production operations require that it obtain adequate supplies of raw materials, such as silicon wafers, gases, chemicals and photoresist, on a timely basis. In the past, shortages in the supply of some materials, whether by specific vendors or by the semiconductor industry generally, have resulted in occasional industry-wide price adjustments and delivery delays. Also, since TSMC procures some of its raw materials from sole-source suppliers, there is a risk that its need for such raw materials may not be met when needed or that back-up supplies may not be readily available. The Company's revenue and earnings could decline if it is unable to obtain adequate supplies of the necessary raw materials in a timely manner or if there are significant increases in the costs of raw materials that it cannot pass on to its customers.

To reduce the supply chain risk and to manage the cost actively, TSMC is committing resources toward developing new supply sources. In addition, the Company encourages its suppliers to reduce their supply chain risk by decentralizing production plants, and to intensify their cost competitiveness by moving their production site to Taiwan from high-cost areas. The Company believes this benefits both suppliers and TSMC. Moreover, the Company continually refines its planning system and monitors its inventory and replenishment on a daily basis so as to sustain an optimal level at rational cost.

- Equipment

The Company's operations and ongoing expansion plans depend on its ability to obtain an appropriate amount of equipment and related services from a limited number of suppliers in a market that is characterized from time to time by limited supply and long delivery cycles. During such times, supplier-specific or industry-wide lead times for delivery can be as long as six months or more. To better manage its supply chain, the Company has implemented various business models and risk management contingencies with suppliers to shorten the procurement lead time. TSMC also provides its projected demand for various items to many of its equipment suppliers to help them plan their production in advance. The Company has purchased used tools and continues to seek opportunities to acquire relevant used tools. Further, the growing complexities especially in next-generation lithographic technologies may delay the timely availability of the equipment and parts needed to exploit time sensitive business opportunities and also increase the market price for such equipment and parts. If TSMC is unable to obtain equipment in a timely manner to fulfill its customers' orders, or at a reasonable cost, its financial condition and results of operations could be negatively impacted.

Risks Associated with Intellectual Property Rights

The Company's ability to compete successfully and to achieve future growth will depend in part on the continued strength of its intellectual property portfolio. While TSMC actively obtain, preserve, enforces, defend and protects its intellectual property rights, there can be no assurance that its efforts will be adequate to prevent the misappropriation or improper use of its proprietary technologies, trade secrets, software or know-how. Also, the Company cannot assure that, as its business or business models expand into new areas, or otherwise, it will be able to develop independently the technologies, trade secrets, patents, software or know-how necessary to conduct its business or that it can do so without unknowingly infringing the intellectual property rights of others. As a result, TSMC may have to rely increasingly on licensed technologies and patent licenses from others. To the extent that the Company relies on licenses from others, there can be no assurance that it will be able to obtain any or all of the necessary licenses in the future on terms it considers reasonable or at all. The lack of necessary licenses could expose TSMC to claims for damages and/or injunctions from third parties, as well as claims for indemnification by its customers in instances where it has contractually agreed to indemnify its customers against damages resulting from infringement claims.

TSMC has received, from time-to-time, communications from third parties asserting that its technologies, manufacturing processes, the design of the integrated circuits made by TSMC or the use by its customers of semiconductors made by TSMC may infringe upon their patents or other intellectual property rights. Because of the nature of the industry, the Company may continue to receive such communications in the future. In some instances, these disputes have resulted in litigation. Recently, there has been a notable increase in the number of claims or lawsuits initiated by certain patent assertion entities and these entities are also becoming more aggressive in their monetary demands and requests for court-issued injunctions. Such lawsuits or claims may increase TSMC's cost of doing business and may potentially be extremely disruptive if the plaintiffs succeed in blocking the trade of its products and services. If TSMC fails to obtain or maintain certain government, technologies or intellectual property licenses and, if litigation related to alleged intellectual property matters occurs, it could prevent it from manufacturing or selling particular products or applying particular technologies, which could reduce its opportunities to generate revenues.

TSMC has taken other measures to minimize potential loss of shareholder value arising from intellectual property claims and litigation filed against the Company. These measures include: obtaining licenses from certain semiconductor and other technology companies; timely securing of intellectual property rights for defensive and/or offensive protection of TSMC technology and business; aggressively defending against frivolous litigation; and acquiring or licensing strategic intellectual property rights necessary to protect its technologies and business offerings.

Risks Associated with Litigation

As is the case with many companies in the semiconductor industry, TSMC has received from time-to-time communications from third parties asserting that its technologies, manufacturing processes, the design of the integrated circuits made by it or the use by its customers of semiconductors made by it may infringe upon patents or other intellectual property rights of others. In some instances, these disputes have resulted in litigation by or against the Company and certain settlement payments by it in some cases. Irrespective of the validity of these claims, TSMC could incur significant costs in the defense thereof or could suffer adverse effects on its operations.

In June 2010, Keranos, LLC. filed a complaint in the U.S. District Court for the Eastern District of Texas alleging that TSMC, TSMC North America, and several other leading technology companies infringe three expired U.S. patents. In response, TSMC, TSMC North America, and several co-defendants in the Texas case filed a lawsuit against Keranos in the U.S. District Court for the Northern District of California in November 2010, seeking a judgment declaring that they did not infringe the asserted patents, and that those patents are invalid. These two litigations have been consolidated into a single lawsuit in the U.S. District Court for the Eastern District of Texas. In February 2014, the Court entered a final judgment in favor of TSMC, dismissing all of Keranos' claims against TSMC with prejudice.

In December 2010, Ziptronix, Inc. filed a complaint in the U.S. District Court for the Northern District of California accusing TSMC, TSMC North America and one other company of infringing several U.S. patents. The outcome cannot be determined at this time.

In December 2013, Tela Innovations, Inc. filed complaints in the U.S. District Court for the District of Delaware and in the United States International Trade Commission accusing TSMC and TSMC North America of infringing one U.S. patent. The Delaware case had been stayed since February 2014. In January 2014, TSMC filed a lawsuit in the U.S. District Court for the District of North California against Tela for trade secret misappropriation and breach of contract. The outcome cannot be determined at this time.

Other than the matters described above, TSMC was not involved in any other material litigation in 2013 and are not currently involved in any material litigation.

Risks Associated with Mergers and Acquisitions

As of the date of this Annual Report, there were no such risks for TSMC.

Risks Associated with Recruiting and Retaining Qualified Personnel

The Company depends on the continued services and contributions of its executive officers, skilled technical personnel, personnel of other expertise and direct labors. TSMC's business could suffer if it loses, for whatever reasons, the services and contributions of some of these personnel and it cannot adequately replace them. The Company may be required to increase or reduce the number of employees in connection with any business expansion or contraction, in accordance with market demand for its products and services. Since there is intense competition for the recruitment of these personnel, the Company cannot ensure it will be able to fulfill its personnel requirements in a timely manner during an economic upturn. However, no such incident has happened to TSMC as of the date of this annual report.

TSMC provides a varied and competitive compensation programs, and is generous in sharing the Company's long-term business achievements with its employees. Furthermore, in order to attract and retain talents, the Company is dedicated to providing a timely distribution of employees' cash bonus from its profits. TSMC believes that by rewarding employees' hard work in a timely fashion, it not only encourages employees to contribute consistently to ensure the success of the Company, but also links their interests with those of TSMC's shareholders.

Future R&D Plans and Expected R&D Spending

For additional details, please refer to "*5.2.7 Future R&D Plans*" on page 66 of this Annual Report.

Changes in Corporate Image and Impact on Company's Crisis Management

TSMC has established an excellent corporate image around the world based on its core values of "Integrity, Commitment, Innovation, and Customer Trust," as well as its outstanding operations, rigorous corporate governance, and dedication to corporate social responsibility to pursue sustainable development, equality and justice, and a harmonious society to live and work.

TSMC was honored with awards for its achievements in operations, corporate governance, innovation, profit growth, investor relations, and corporate social responsibility and other fields in 2013, further strengthening the Company's public reputation. In addition to being selected as a component of the Dow Jones Sustainability Index (DJSI) for a 13th consecutive year, TSMC was also recognized by DJSI as the Semiconductors and Semiconductor Equipment Industry Group Leader. TSMC is the first Taiwan company, and one of just four Asian companies, to win the highest score out of its industry peers in the DJSI's 24 industry groups.

In addition, in 2013 TSMC received the R.O.C. Executive Yuan National Sustainable Development Award, National Industrial Innovation Award, Environmental Protection Administration (EPA) National Enterprise Environmental Protection Award, the EPA Energy Conservation and Carbon Reduction Action Mark, the Science Park Low-Carbon Enterprise Achievement Award, the Science Park Labor Health and Safety Achievement Award, and the Taiwan Institute for Sustainable Energy 2013 Taiwan Corporate Sustainability Award. TSMC was also recognized as the Most Admired Company in Taiwan by *CommonWealth Magazine*, won the CommonWealth Corporate Citizenship Award, and placed number one in the magazine's ranking of the most profitable manufacturing companies in Taiwan.

TSMC took the first prize in the Occupational Health category for the *GlobalViews Magazine* Corporate Social Responsibility Award, was ranked number one in net profit and profitability in the China Credit Information Service poll of major corporations in Taiwan, and also ranked first in the *Business Next Magazine* "Infotech 100" for Taiwan and Asia. TSMC was one of *Barron's* Magazine's "Top 100 World's Most Respected Companies" in 2013, and received the "Best-Managed Company in Asia," "Best Corporate Governance, Taiwan," and "Best Corporate Social Responsibility, Taiwan" Awards from *FinanceAsia*.

TSMC has always endeavored to act as a positive force in society, and maintains departments such as Brand Management, Customer Service, Public Relations, Employee Relations, Investor Relations, Risk Management, Fab Industrial Safety and Environmental Protection, Internal Audit, and the TSMC Foundation to coordinate the Company's resources and further enhance TSMC's positive corporate image.

To address potential events that may affect the Company's public image, including natural disasters, fires, workplace accidents, power outages, water shortages and workplace injuries, TSMC maintains an Emergency Response Procedure Manual, and health and safety supervisors for each fab hold meetings of the "Environment, Health, and Safety Technical Board" every month. In addition, relevant departments hold regular drills and continuously improve their emergency response and notification procedures. At the same time, TSMC has established communications criteria for all types of stakeholders, and the Public Relations Department is responsible for external communications. In the event of emergencies, rapid deployment of emergency response reduces casualties and minimizes impact on the surrounding environment, company property, and manufacturing operations. The Public Relations Department's involvement at the first stage of response also ensures smooth channels of communications to maintain the Company's image.

Risks Associated with Change in Management

The Board of Directors approved the appointment of Drs. Mark Liu and C.C. Wei (in alphabetical order) as President and Co-Chief Executive Officer of TSMC at its meeting of November 12, 2013. Dr. Morris Chang remains as the Chairman of TSMC. The Presidents and the Co-Chief Executive Officers shall report to and perform such duties as designated by the Chairman of the Board. Finance and Legal organizations will continue to report to the Chairman.

6.2.4 Financial Risks

Internal Management of Economic Risks

- Interest Rate Fluctuation

TSMC's exposure to interest rate risks derives primarily from short-term borrowing and long-term debt obligations incurred in the normal course of business. In order to limit its exposure to interest rate risks, TSMC finances its funding needs primarily through internal generation of cash and the issuance of long-term, fixed-rate debt. On the asset side, we place our cash on hand mainly in very short tenor time deposits. Furthermore, the primary objective of TSMC's cash investments in fixed income securities is to preserve principal in highly liquid markets. In order to maintain the Company's liquidity profile, the majority of fixed income securities are at the short end of the yield curve.

- Foreign Exchange Volatility

More than half of TSMC's capital expenditures and manufacturing costs are denominated in currencies other than NT dollars, primarily in US dollars, Japanese yen and Euros. In 2013, more than 90% of the Company's sales were denominated in US dollars and currencies other than NT dollars. Therefore, any significant fluctuation to its disadvantage in such exchange rates would have an adverse effect on TSMC's financial condition. For example, during the period from September 1, 2010 to December 30, 2010, the US dollar depreciated 8.9% against the NT dollar, which had a negative impact on the Company's results of operations. Specifically, based on TSMC's 2013 results, every 1% depreciation of the US dollar against the NT dollar exchange rate may result in approximately 0.4 percentage point decrease in TSMC's operating margin. TSMC utilizes short-term debt denominated in foreign currencies and derivative financial instruments, including currency forward contracts and cross currency swaps, to hedge our currency exposure.

Fluctuations in the exchange rate between the US dollar and the NT dollar may affect the US dollar value of the Company's common shares and the market price of the Company's American Depositary Shares (ADSs) and of any cash dividends paid in NT dollars on TSMC's common shares represented by ADSs.

- Inflation and Deflation

The world economy is becoming more vulnerable to sudden unexpected fluctuations in inflationary and deflationary market expectations and conditions. For example, certain structural changes that resulted from the global financial crisis in 2008~2009 and EU sovereign debt crises, such as highly accommodative monetary policies by major central banks worldwide, may cause variations in the expectation of inflation or deflation. Both high inflation and deflation adversely affect an economy, at both the macro and micro levels, by reducing economic efficiency, disrupting saving and investment decisions and reducing the efficiency of the market prices as a mechanism to allocate resources. Such fluctuations may negatively affect the costs of TSMC's operations and the business operations of its customers who may be forced to plan their purchases of TSMC's goods and services within an uncertain macro and micro economy. Therefore, the demand for TSMC's products and services could unexpectedly fluctuate severely in accordance with market and consumer expectations of inflation or deflation.

Risks Associated with External Financing

Capital requirements are difficult to plan in the highly dynamic, cyclical and rapidly changing semiconductor industry. From time to time – and increasingly so for the foreseeable next few years – TSMC will continue to need significant capital to fund its operations and manage its capacity in accordance with market demand. TSMC's continued ability to obtain sufficient external financing is subject to a variety of uncertainties, including:

- its future financial condition, results of operations and cash flow;
- general market conditions for financing activities;
- market conditions for financing activities of semiconductor companies; and,
- social, economic, financial, political and other conditions in Taiwan and elsewhere.

Sufficient external financing may not be available to the Company on a timely basis, on reasonable market terms, or at all. As a result, TSMC may be forced to curtail its expansion and modification plans or delay the deployment of new or expanded services until it obtains such financing.

Risks Associated with High-risk/high-leveraged Investment; Lending, Endorsements, and Guarantees for Other Parties; and Financial Derivative Transactions

TSMC did not make high-risk or high-leveraged financial investments during 2013 and up to the date of this report. TSMC provided a guarantee to TSMC Global, a wholly-owned subsidiary of TSMC, for its issuance of US dollar-denominated senior unsecured corporate bonds of US$1,500 million in April 2013. As of February 28, 2014, TSMC had an intercompany loan of US$100 million arranged among the Company's subsidiaries, which was in compliance with relevant rules and regulations.

The financial transactions of a "derivative" nature that TSMC entered into were strictly for hedging purposes and not for any trading or speculative purpose. For more information, please refer to pages 27 and 28 of the Annual Report section (II), Financial Information. The fair market value of our trading and available-for-sale financial securities are subject to prevailing market conditions and may fluctuate from TSMC's carrying value from time to time, which may impact the returns of those securities.

To control various types of financial transactions, the Company has established internal policies and procedures based on sound financial and business practices, all in compliance with the relevant rules and regulations issued by the Taiwan Securities and Futures Bureau. TSMC policies and procedures include "Policies and Procedures for Financial Derivative Transactions," "Procedures for Lending Funds to Other Parties," "Procedures for Acquisition or Disposal of Assets," and "Procedures for Endorsement and Guarantee".

Risks Associated with Strategic Investments

From time to time, TSMC has made or will make a series of strategic investments that serve two major purposes. First, some of TSMC's major strategic investments were, or will be, made to help the Company open new sources of revenues and innovate alternative business models that target to generate additional shareholders' value going forward in the future. For example, in order to help the Company grow into next generation business areas, TSMC has invested to develop potential businesses in solid state lighting, solar power and other renewable sources of energy. The Company believes these investments into these areas will generate new sources of revenues as a gradual transition into consuming cleaner sources of power is generally expected. For further information on these investments, please refer to "*8. Subsidiary Information and Other Special Notes*" on pages 110-115 of this Annual Report. Second, some of TSMC's significant strategic investments were, or will be, made to help the Company grow its existing business by augmenting key technology development. For example, to accelerate the development of next-generation lithographic technology, in August 2012, TSMC, along with other major technology firms, joined the ASML Holding N.V. Customer Co-Investment Program. The program's scope includes development of extreme ultraviolet (EUV) lithography technology and 450-millimeter (450mm) lithography tools. Under the agreement with ASML, TSMC invested EUR838 million to acquire 5% of ASML's equity and has committed EUR276 million, to be spread over five years, toward ASML's research and development program. As a result, the Company is exposed to share price fluctuations arising from its investment in ASML. In the future, TSMC may make more strategic investments in various forms, whether through stock purchases, assets purchases, licensing of major intellectual property rights, joint investments or research and development projects, outright mergers and acquisitions, private equity transactions and other similar transactions. Any such investment will incur risks, which may result in losses if not carefully managed. Any such loss resulting from such investments may result in significant impairment charges, lower profit margin and ultimately lower distributable earnings.

Risks Associated with Impairment Charges

Under Taiwan-IFRSs, TSMC is required to evaluate its investments, tangible and intangible assets for impairment whenever triggering events or changes in circumstances indicate that the asset may be impaired. If certain criteria are met, TSMC is required to record an impairment charge. TSMC is also required under Taiwan-IFRSs to evaluate goodwill for impairment at least on an annual basis or more frequently whenever triggering events or changes in circumstances indicate that goodwill may be impaired and the carrying value may not be recoverable. For example, TSMC holds investments in certain publicly listed and private companies, some of which have incurred certain impairment charges disclosed in the "Financial Information" of Annual Report (II), pages 28-30.

The determination of an impairment charge at any given time is based on the expected results of the Company's operations over a number of years subsequent to that time. As a result, an impairment charge is more likely to occur during a period when the Company's operating results are otherwise already depressed.

TSMC has established the process and system to closely monitor and assess the risk of any impairment charge. However, the management is unable to estimate the extent or timing of any impairment charge for future years, or whether such impairment charge required may have a material adverse effect on the Company's net income.

6.2.5 Hazardous Risks

TSMC maintains a comprehensive risk management system dedicated to the conservation of natural resources, the safety of people, and the protection of property. In order to effectively handle emergencies and natural disasters at each facility, management has developed comprehensive plans and procedures that focus on risk prevention, emergency response, crisis management, and business continuity. TSMC has adopted local and international standards for Environmental, Safety and Health (ESH) management. All TSMC manufacturing fabs have been ISO 14001 certified (Environmental Management System), OHSAS 18001 certified (Occupational Health and Safety Management System) and QC 080000 certified (Hazardous Substance Process Management System). All manufacturing fabs in Taiwan have also been TOSHMS (Taiwan Occupational Safety and Health Management System) certified. The new fabs will also acquire the above certificates within 18 months after volume production.

The Company pays special attention to preparedness for emergencies or disasters, such as typhoons, floods, droughts caused by climate change, earthquakes, environmental contamination, large-scale product returns, service disruption of IT systems, strikes, pandemics (such as H1N1 influenza), and sudden and unexpected disruptions to the supply of raw materials or water, electricity, and other public utilities. TSMC has established a company-wide task force dedicated to managing the risk of water shortage that might arise due to climate change. This task force keeps watch on the external supply and internal demand for water. Cross-company consolidations and external collaborations with public agencies are also ongoing in the industrial parks to ensure and sustain a stable water supply.

TSMC has further strengthened its business continuity plans, which include periodic risk assessment, risk mitigation, and implementation through the establishment of emergency task forces when necessary, combined with the preparation of a thorough analysis of the emergency, its impact, alternative actions, and solutions for each possible scenario together with appropriate precautionary and/or recovery measures. Each task force is given the responsibility of ensuring TSMC's ability to conduct business while minimizing personal injury, business disruption, and financial impact under the circumstances. TSMC's business continuity plan is periodically reviewed according to results of test scenarios or practical implementation for ensuring effective and successful business continuity. Customers are informed of TSMC's strong business continuity capability in order to establish resilience and flexibility in both their supply chain and insurance placement. For the year 2013, and up to the date of this Annual Report, there have been no reportable material events that have necessitated the activation of such contingency plans.

The Company has also conducted a continuous improvement project, including evaluating building anti-seismic capability, holding earthquake emergency response drills, enhancing tool anchorage or seismic isolation facilities, training and preparedness for tool salvage, and has improved TSMC business continuity procedures with reference to ISO 22301 business continuity management.

TSMC and many of its suppliers use highly combustible and toxic materials in its manufacturing processes and are therefore subject to the risk of loss arising from explosion, fire, or environmental influences which cannot be completely eliminated. Although the Company maintains many overlapping risk prevention and protection systems, as well as comprehensive fire and casualty insurance, including insurance for loss of property and loss of profit resulting from business interruption, TSMC's risk management and insurance coverage may not be sufficient to cover all of the Company's potential losses. If any of TSMC's fabs or vendor facilities were to be damaged, or cease operations as a result of an explosion, fire or environmental influences, it could reduce the Company's manufacturing capacity and may cause it to lose important customers, thereby having a potentially adverse and material impact on TSMC's financial performance. In addition to periodic fire protection system inspection and firefighting drills, the Company has also carried out a corporate-wide fire risk mitigation project focused on management and hardware improvements.

Changes may cause unpredictable interruption to production. In order to reduce such uncertainty, TSMC has adopted a number of standards to maintain operational continuity, ranging from design, procurement and construction of facilities, to operation and decommission.

6.2.6 Risks Associated with Climate Change and Non-compliance with Environmental and Climate Related Laws and Regulations, and Other International Laws, Regulations and Accords

The manufacturing, assembling and testing of our products require the use of metals, chemicals and materials that are subject to environmental, climate-related, health and safety and humanitarian, conflict-free sourcing laws, regulations and guidelines issued worldwide. For example, the U.S. SEC implemented the final rule mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act to require companies to publicly disclose their use of conflict minerals (i.e. Gold, Cassiterite, Coltan and Wolframite) that originated in the Democratic Republic of the Congo (DRC) or an adjoining country. The final applicable legal rule as well as non-binding guidelines on conflict minerals imposes substantial supply chain verification requirements in the event that conflict minerals originates from the Democratic Republic of the Congo, adjoining countries or any geographic territory that may be specified by the relevant authorities at a future date. These new rules and verification requirements, which apply to our activities in 2013 and beyond, impose additional costs on us and on our suppliers and may limit the sources or increase the prices of materials used in our products. Further, if we are unable to certify that our products are conflict free under applicable law or non-binding guidelines or if we are unable to comply with any material provisions of such laws or guidelines, we may face challenges with our customers that place us at a significant competitive disadvantage, and our goodwill and

reputation may be irreparably damaged. Often times, our customers have imposed upon us legally non-binding conditions or guidelines on sourcing conflict minerals that exceed those imposed under relevant legal requirements. For example, many of our customers have been asking us to apply the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals in Conflict-Affected and High-Risk Areas. These guidelines while legally non-binding may impose requirements that well exceed those mandated by applicable law. If we agree to apply these guidelines as requested by our customers, there is the risk that the prices we charge for our products and services will increase (to reflect the added cost in complying with such conditions or guidelines), resulting in the loss of actual and potential customers. Conversely, any failure on our part to comply with such customer-imposed legally non-binding conditions or guidelines may result in us suffering significant competitive harms such as the loss of actual or potential customers that will likely have a material adverse impact on our financial statements.

Although TSMC may be eligible for various exemptions and/or extensions of time for compliance, our failure to comply with any of these applicable laws or regulations could result in:

- significant penalties and legal liabilities, such as the denial of import permits;
- the temporary or permanent suspension of production of the affected products;
- unfavorable alterations in our manufacturing, fabrication and assembly and test processes;
- loss of actual or potential sales contracts in case we are unable to satisfy the conditions regarding conflict-free minerals sourcing laws or requirements by our customers; and
- restrictions on our operations or sales

Existing and future environmental and climate related laws and regulations as well as applicable international accords to which TSMC are subject, could also require it, among other things, to do the following: (a) purchase, use or install expensive pollution control, reduction or remediation equipment; (b) implement climate change mitigation programs and "abatement or reduction of greenhouse gas emissions" programs, or "carbon credit trading" programs; (c) modify our product designs and manufacturing processes, or incur other significant expenses associated with such laws and regulations such as obtaining substitute raw materials or chemicals that may cost more or be less available for our operations. It is unclear whether such necessary actions would affect the reliability or efficiency of our products and services.

Any of the above contingencies resulting from the actual and potential impact of local or international laws and regulations, as well as international accords on environmental or climate change, could harm the Company's business and operational results by increasing expenses or requiring TSMC to alter its manufacturing, assembly and test processes.

Increasing climate change and environmental concerns could affect the results of our operations if any of our customers request that we provide products and services that exceed any existing standard(s) of environmental compliance. For example, TSMC has been working on an on-going basis with our suppliers, customers, and several industry consortia to develop and provide products that are compliant with the European Union Restriction of Hazardous Substances Directive (RoHS). Even though TSMC is entitled to rely on various exemptions under RoHS, some of our customers may request that we provide products that exceed the legal standard set by RoHS without using any of the exemptions still permitted under RoHS. If TSMC is unable to offer such products or offer products that are compliant, but are not as reliable due to the lack of reasonably available alternative technologies or materials, it may lose market share to our competitors.

Further, energy costs in general could increase significantly due to climate change and other regulations. Therefore, TSMC's energy costs may increase significantly if utility or power companies pass on their costs, either fully or partially, such as those associated with carbon taxes, emission caps and carbon credit trading programs.

TSMC believes that climate change should be regarded as an important corporate risk, which must be controlled to improve our competitiveness. Climate change risks include legal risk, physical risk and other risks. TSMC's control measures are as follows:

- Climate Regulatory Risk Control

The greenhouse gas (GHG) control regulations and agreements of countries around the world are becoming more and more stringent. Enterprises are legally required to regularly disclose GHG-related information, and also limit GHG emissions. The cost of production, including materials and energy, may also grow along with future legal requirements such as carbon or energy taxes. TSMC continues to monitor legislative trends and communicate with various governments through industrial organizations and associations to set reasonable and feasible legal requirements.

- Conflict Minerals Risk Control

For additional details, please refer to the section of "Supplier and Contractor Management" of "*7.2.3 Safety and Health*" on pages 102-104 of this Annual Report.

- Climate Disaster Risk Control

Abnormal climate caused by the greenhouse effect has increased the frequency and severity of climate disasters – storms, floods, drought, and water shortages – causing considerable impacts on business operations and supply chains. TSMC believes that climate change control should take into account both mitigation and adaption, and this requires cooperation between industry and government to reduce risk. To ensure electricity and raw water supplies, therefore, in addition to water-saving measures at our own facilities and those of our upstream and downstream partners, TSMC participates in the Taiwan Science Park Industrial Union Experts Committee platform, and is actively involved in regular meetings with Taipower Company and the Taiwan Water Corporation to discuss supply and allocation for response issues.

- Other Climate Risk Controls

Climate change is a concern to the global supply chain, necessitating energy conservation, carbon reduction, and disaster prevention. For example, The Electronic Industry Citizenship Coalition (EICC) has also required members' suppliers to disclose GHG emissions information. TSMC not only discloses its own GHG emissions information each year, but it also assists and requires its suppliers to establish a GHG inventory system and conduct reduction programs. TSMC's suppliers are required by TSMC to submit GHG emissions and reduction information as an important index of sustainability scoring in its procurement strategy.

To mitigate risks resulting from climate change, TSMC continues to actively carry out energy conservation measures, and voluntary perfluorinated compounds (PFC) emission reduction projects and conducting GHG inventory and verification every year. TSMC has publicly disclosed climate change information every year through the following channels:

- TSMC has disclosed GHG emissions and reduction-related information for evaluation by the Dow Jones Sustainability Index every year since 2001.
- TSMC's GHG-related information has been disclosed in its CSR report on the Company website annually since 2008. TSMC also provides information to customers and investors upon request.
- Since 2005, TSMC has been participating in an annual survey held by the nonprofit Carbon Disclosure Project (CDP), which includes GHG emission and reduction information for all TSMC fabs, subsidiaries, joint ventures, and overseas offices.
- Since 2006, TSMC follows the ISO 14064-1 standard to conduct a GHG inventory and acquire verification by an accreditation agency every year. TSMC also voluntarily reports GHG inventory data to the Taiwan Environmental Protection Administration (EPA) and the Taiwan Semiconductor Industry Association (TSIA).

6.2.7 Other Risks

Potential Impact and Risks Associated with Sales of Significant Numbers of Shares by TSMC's Directors, and/or Major Shareholders Who Own 10% or More of TSMC's Total Outstanding Shares

The value of TSMC shareholders' investment may be reduced by possible future sales of TSMC shares owned by the major shareholders.

One or more of our existing shareholders may, from time to time, dispose of significant numbers of our common shares or ADSs. For example, the National Development Fund, which owned 6.38% of TSMC's outstanding shares as of February 28, 2014, has from time to time in the past sold our shares in the form of ADSs in several transactions.

Currently no shareholder owns 10% or more of TSMC's total outstanding shares.

Other Material Risks

During 2013 and as of the date of this Annual Report, TSMC's management is not aware of any other risk event that could impart a potentially material impact on the financial status of the Company.