

COLORSTARS GROUP

CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

June 30, 2015

COLORSTARS GROUP
CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANT

COLORSTARS GROUP
CONSOLIDATED BALANCE SHEETS
(UnAUDITED)
(IN US\$)

	June 30, 2015	December 31, 2014
<u>Assets</u>		
Current assets:		
Cash and equivalents	\$108,000	\$75,397
Accounts receivable, net of allowance for doubtful accounts of \$57,071 at June 30, 2015 and \$53,327 at December 31, 2014 Net of due from affiliate account of \$556,259 at June 30, 2015 and \$372,549 at December 31, 2014.	153,001	449,703
Inventory	619,637	664,444
Prepaid expenses and other current assets	61,952	48,103
	942,590	1,237,647
Equipment, net of accumulated depreciation	80,910	81,958
Investments	154,917	137,767
Other assets	20,013	26,496
	\$1,198,430	\$1,483,868
<u>Liabilities and stockholders' equity</u>		
Current liabilities:		
Short term loan	\$549,765	\$537,651
Accounts payable	194,085	404,319
Accrued expenses	16,130	21,366
Receipts in advance and other current liabilities	80,689	17,038
	840,669	980,374
Commitments and contingencies		
Stockholders' equity		
Common Stock –Par Value \$0.001 67,448,890 shares issued and outstanding at June 30, 2015 and December 31, 2014	67,449	67,449
Additional paid in capital	3,112,230	3,112,230
Accumulated other comprehensive income	253,532	198,581
Accumulated deficit	(3,075,450)	(2,874,766)
	357,761	503,494
Total liabilities and stockholders' equity	\$1,198,430	\$1,483,868

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

COLORSTARS GROUP
CONSOLIDATED STATEMENTS OF OPERATION AND COMPREHENSIVE LOSS
(UNAUDITED)
(IN US\$)

	Three months ended June 30,	
	2015	2014
Net sales	\$380,874	\$287,755
Cost of goods sold	414,467	203,590
Gross profit	(33,593)	84,165
Operating expenses		
Selling, general and administrative	124,394	135,488
Research and development	715	5,983
Total operating expenses	125,109	141,471
Loss from operations	(158,702)	(57,306)
Other income (expenses)		
Interest expense (net)	(2,636)	(2,352)
Share of investee's operating results (net)	-	-
Gain (loss) on foreign exchange, net	(6,424)	(13,077)
Other, net	-	(3,256)
Loss before income tax	(167,762)	(75,991)
Income tax benefit (expense)	677	2,027
Net loss	(167,085)	(73,964)
Earnings per share attributable to common stockholders:		
Basic and diluted per share	\$0.00	\$0.00
Weighted average shares outstanding:		
Basic and diluted	67,448,890	67,448,890
Comprehensive loss:		
Net loss	(167,085)	(73,964)
Other comprehensive loss:		
Foreign currency translation gain(loss), net of taxes	84,351	32,081
Comprehensive loss	\$(82,734)	\$(41,883)

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

COLORSTARS GROUP
CONSOLIDATED STATEMENTS OF OPERATION AND COMPREHENSIVE LOSS
(UNAUDITED)
(IN US\$)

	Six months ended June 30,	
	2015	2014
Net sales	\$570,489	\$499,844
Cost of goods sold	498,177	357,616
Gross profit	72,312	142,228
Operating expenses		
Selling, general and administrative	257,237	289,022
Research and development	705	5,965
Total operating expenses	257,942	294,987
Loss from operations	(185,630)	(152,759)
Other income (expenses)		
Interest expense (net)	(5,892)	(4,245)
Share of investee's operating results (net)	-	(54,815)
Gain (loss) on foreign exchange, net	(18,782)	(2,475)
Other, net	533	2,742
Loss before income tax	(209,771)	(211,552)
Income tax benefit (expense)	9,087	3,689
Net loss	(200,684)	(207,863)
Earnings per share attributable to common stockholders:		
Basic and diluted per share	\$0.00	\$0.00
Weighted average shares outstanding:		
Basic and diluted	67,448,890	67,448,890
Comprehensive loss:		
Net loss	(200,684)	(207,863)
Other comprehensive loss:		
Foreign currency translation gain(loss), net of taxes	54,951	(25,420)
Comprehensive loss	\$(145,733)	\$(233,283)

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

COLORSTARS GROUP
CONSOLIDATED STATEMENT OF CASH FLOWS
(UnAUDITED)
(IN US\$)

	For three months ended June 30,	
	2015	2014
Cash flows from operating activities		
Net (loss)	\$(167,085)	\$(73,964)
Depreciation and amortization	8,848	9,621
Provision for doubtful accounts	5,091	-
Changes in operating assets and liabilities:		
Accounts receivable	89,834	(18,482)
Inventories	114,170	(14,783)
Prepaid expenses and other current assets	(5,327)	7,841
Accounts payable	(147,017)	21,895
Accrued expenses	(3,227)	(34,627)
Receipts in advance and other current liabilities	(1,857)	2,376
Cash flows (used in) operating activities	<u>(106,570)</u>	<u>(100,123)</u>
Cash flows from investing activities		
Addition to fixed assets	<u>(10,314)</u>	-
Cash flows provided from (used in) investing activities	<u>(10,314)</u>	-
Effect of exchange rate changes on cash and cash equivalents	<u>80,891</u>	<u>23,965</u>
Net (decrease) in cash and cash equivalents	(35,993)	(76,158)
Beginning cash and cash equivalents	<u>143,993</u>	<u>192,493</u>
Ending cash and cash equivalents	<u><u>108,000</u></u>	<u><u>\$116,335</u></u>
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Interest	\$2,700	\$2,414
Tax paid	(3)	(2,026)

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

(UNAUDITED)
(IN US\$)

	For six months ended June 30,	
	2015	2014
Cash flows from operating activities		
Net (loss)	\$(200,684)	\$(207,863)
Depreciation and amortization	17,312	18,561
Gain on disposal of investment	-	-
Provision for doubtful accounts	2,520	2,300
Share of investment loss	-	54,815
Changes in operating assets and liabilities:		
Accounts receivable	294,182	22,178
Inventories	44,807	8,259
Prepaid expenses and other current assets	(11,404)	10,874
Accounts payable	(210,234)	(90,872)
Accrued expenses	(5,236)	(3,593)
Receipts in advance and other current liabilities	63,651	5,120
Cash flows (used in) operating activities	(5,086)	(180,221)
Cash flows from financing activities		
Increase in short-term loans	-	99,947
Cash flows provided from (used in) financing activities	-	99,947
Cash flows from investing activities		
Addition to fixed assets	(10,175)	-
Cash flows provided from (used in) investing activities	(10,175)	-
Effect of exchange rate changes on cash and cash equivalents	47,864	9,652
Net (decrease) in cash and cash equivalents	32,603	(70,622)
Beginning cash and cash equivalents	75,397	186,957
Ending cash and cash equivalents	\$108,000	\$116,335
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Interest	\$5,921	\$4,309
Tax paid	(3)	(3,689)

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

COLORSTARS GROUP AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Nature of Business and Basis of Presentation

Nature of Business – Circletronics Inc., now ColorStars Group (“the Company”), was incorporated in Canada on January 21, 2005. Circletronics Inc.- was redomiciled to Nevada and its name changed to ColorStars Group on November 3, 2005. ColorStars Group owns 100% of the shares of ColorStars Inc.

Color Stars Inc. (“Color Stars TW”, “the Subsidiary”) was incorporated as a limited liability company in Taiwan, Republic of China in April 2003 and commenced its operations in May 2003. The Subsidiary is mainly engaged in manufacturing, designing and selling light-emitting diode and lighting equipment.

Basis of Presentation - The accompanying unaudited consolidated financial statements of ColorStars Group and Color Stars Inc. (“the Company”) have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to the Quarterly Report on Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for a complete presentation of the financial statements.

In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for fair statement of the financial position, results of operations and cash flows for the six months ended June 30, 2015 and 2014 have been included. For further information, refer to the consolidated financial statements and footnotes included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2014. Operating results for the six months ended June 30, 2015 are not necessarily indicative of the results to be expected for any subsequent interim period or for the year ending December 31, 2015.

Basis of Consolidation - The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated.

Note 2 - Recent Adopted Accounting Pronouncements

Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income - In February 2013, the Financial Accounting Standards Board (“FASB”) issued ASU 2013-02, which requires disclosure of significant amounts reclassified out of accumulated other comprehensive income by component and their corresponding effect on the respective line items of net income. This guidance is effective for the Company beginning in the first quarter of 2013. The adoption of ASU 2013-02 only impacted disclosure requirements and did not have any effect on the operating results or the financial condition.

COLORSTARS GROUP AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 3 - Recently Issued Accounting Pronouncements

Foreign Currency Matters – Effective December 15, 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2013-05, *Foreign Currency Matters*. The parent entity is required to release any related cumulative translation adjustment into net income when the entity ceases to have a controlling financial interest in a subsidiary or group of assets. A pro rata portion of the cumulative translation adjustment should be released into net income upon a partial sale of such an equity method investment.

Note 4 - Concentration of Risk

Financial instruments that potentially subject the Company to significant concentration of credit risk consist principally of accounts receivable, cash and cash equivalents. The Company's cash and cash equivalents are maintained with high quality institutions, the compositions and maturities of which are regularly monitored by management. Through June 30, 2015, the Company had not experienced any losses on such deposits.

Accounts receivable include amounts due from customers primarily in the manufactory industry. The Company performs ongoing credit evaluations of its customers' financial condition and limits the amount of credit extended when deemed necessary, but generally requires no collateral. The Company also maintains allowances for potential credit losses. In estimating the required allowances, the Company takes into consideration the overall quality and aging of the receivable portfolio, the existence of a limited amount of credit insurance and specifically identified customer risks. Through June 30, 2015, such losses have been within management's expectations.

For the six months ended June 30, 2015, products sold to the Company's largest customer, accounted for approximately 55.26%. Products purchased from the Company's first two largest suppliers were accounted for approximately 45.61% of the total purchases.

Note 5 - Earnings Per Share

Basic net loss per share is computed by dividing net loss for the period by the weighted average number of shares of common stock outstanding during the period.

The following table sets forth the computation of basic and diluted net loss per share for the periods indicated:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Net loss attributable to common stockholders	\$(167,085)	\$(73,964)	\$(200,684)	\$(207,863)
Weighted average common stock outstanding – Basic and diluted	67,448,890	67,448,890	67,448,890	67,448,890
Earnings per share attributable to common stockholder Basic and diluted	\$.00	\$.00	\$.00	\$.00

Note 6 - Accumulated Other Comprehensive loss

The components of accumulated other comprehensive losses were as follows:

	Foreign currency translation
Balance, December 31, 2014	\$198,581
Foreign currency translation, net of taxes	54,951
	<hr/>
Balance, June 30, 2015	253,532
	<hr/>
Balance, December 31, 2013	261,108
Foreign currency translation, net of taxes	25,420
	<hr/>
Balance, June 30, 2014	\$286,528
	<hr/>

Note 7 - Long Term Investments

	June 30, 2015	December 31, 2014
Cost-method investment – Anteya Technology Corp		
Carrying value of investment at the beginning	\$137,767	\$223,990
Share of associate's loss	-	(54,606)
Exchange difference	17,150	(31,617)
	<hr/>	<hr/>
Carrying value at the end	154,917	137,767
	<hr/>	<hr/>
Equity method investment – Fin-Core Corporation		
Carrying value of investment at the beginning	-	-
Impairment for the year	-	-
Exchange difference	-	-
	<hr/>	<hr/>
Carrying value at the end	-	-
	<hr/>	<hr/>
Net value	\$154,917	\$137,767
	<hr/>	<hr/>

COLORSTARS GROUP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 7 - Long Term Investments (continued)

The Company adopted the provisions of SFAS 157, which require us to determine the fair value of financial assets and liabilities using a specified fair-value hierarchy. The objective of the fair-value measurement of our financial instruments is to reflect the hypothetical amounts at which we could sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date (exit price). SFAS 157 describes three levels of inputs that may be used to measure fair value, as follows:

Level 1 inputs are quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 inputs are unobservable inputs for the asset or liability that are supported by little or no market activity and that are significant to the fair value of the underlying asset or liability.

Anteya Technology Corp (Anteya) is a private company incorporated in Taiwan. The equity interest held by the Company is 17.33% on June 30, 2015.

Fin-Core Corporation (FCC) is a private company incorporated in Taiwan. The number of shares of Fin-Core held by the Company is 57,143 shares, 5.19% at June 30, 2015 and December 31, 2014. The Company recorded the investment in Fin-Core Corporation at cost.

Phocos AG is a private company incorporated in Germany. The equity interest held by the Company is 2.38%. Investment in Phocos AG is stated at cost.

The unaudited financial information of Anteya Technology Corp. as of June 30, 2015 and December 31, 2014 and for the six months ended June 30, 2015 and 2014 (in US dollars) are as follows:

<u>Balance sheet</u>	<u>June 30, 2015</u>	<u>December 31, 2014</u>
Current assets	\$3,182,317	\$3,801,725
Non-current assets	915,013	829,550
Total assets	<u>4,097,330</u>	<u>4,631,276</u>
Current liabilities	1,092,880	2,353,483
Non-current liabilities	1,751,580	1,344,053
Stockholders' equity	<u>1,252,870</u>	<u>933,740</u>
Total stockholders' equity and liabilities	<u>4,097,330</u>	<u>\$4,631,276</u>

Note 7 - Long Term Investments (continued)

<u>Statement of operation</u>	Six months ended June 30,	
	2015	2014
Net sale	\$1,451,200	\$847,200
Cost of goods sold	(1,301,373)	(895,048)
Gross profit	149,827	(47,848)
Operating and non-operating expenses	(572,061)	(494,092)
Net profit (loss)	\$(422,234)	\$(541,940)

Note 8- Inventory

Inventories stated at the lower of cost or market value are as follows:

	June 30, 2015	December 31, 2014
Finished goods	\$808,388	\$849,036
Allowance for Inventory Valuation and Obsolescence Losses	(188,751)	(184,592)
Total	\$619,637	\$664,444

Note 9 - Income Taxes

The Company is subject to U.S. federal income tax as well as income tax in states and foreign jurisdictions. For the major taxing jurisdictions, the tax years 2006 through 2014 remain open for state and federal examination. The Company believes assessments, if any, would be immaterial to its consolidated financial statements. With respect to the foreign jurisdiction, the Company is no longer subject to income tax audits for the year 2014 (inclusive).

The income tax provision information is provided as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Component of income (loss) before income taxes:				
United States	\$(210,663)	\$(33,845)	\$(236,276)	\$(58,249)
Foreign	43,578	(39,849)	35,592	(79,025)
Net loss	\$(167,085)	\$(73,694)	\$(200,684)	\$(207,863)
Provision for income taxes				
Current				
U.S. federal	-	-	-	-
State and local	-	-	-	-
Foreign	\$(677)	\$(2,027)	\$(9,087)	\$(3,689)
Income tax benefit	\$(677)	\$(2,027)	\$(9,087)	\$(3,689)

Note 10 - Accrued Expenses

	June 30, 2015	December 31, 2014
Salaries and allowance	\$11,084	\$10,424
Insurance	5,046	4,841
Tax payable	-	6,101
	<u>\$16,130</u>	<u>\$21,366</u>

Note 11 - Bank Short Term Debt

	June 30, 2015	December 31, 2014
Bank loan payable to Taiwan banks	<u>\$549,765</u>	<u>\$537,651</u>

The Company signed revolving credit agreements with a lending institution. The interest rate on short-term borrowings outstanding as of June 30, 2015 is 1.94% per annum, as of December 31, 2014, interest rate is 1.94% per annum. The short term debt is secured by:

1. personal guarantee from directors
2. the realty property of spouse of directors

Note 12 - Geographic Information

Product revenues for the six months ended June 30, 2015 and 2014 are as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Customers based in:				
Europe	\$110,361	\$133,305	\$108,879	\$267,627
Asia	10,885	31,913	198,147	56,415
United States	259,628	122,537	263,463	174,895
Others	-	-	-	907
	<u>\$380,874</u>	<u>\$287,755</u>	<u>\$570,489</u>	<u>\$499,844</u>

Note 13 - Related Party Transactions

The Company has recorded expenses for the following related party transactions for six months ended

June 30, 2015 and 2014:

	Six months ended June 30,	
	2015	2014
Purchase from Anteya Technology Corp	\$56,661	\$151,705
Rent paid to Mr. Wei-Rur Chen	23,074	23,843

As of the balance sheet date indicated, the Company had the following receivable and liabilities recorded with respect to related party transactions:

	June 30, 2015	December 31, 2014
Anteya Technology Corp		
Due from affiliate (liabilities)	\$(3,934)	\$284,981
Mr. Wei-Rur Chen		
Due from affiliate	(64,678)	-

The Company leases office space from Mr. Wei-Rur Chen which the term for the agreement is from November 2010 to November 2015.

The Company conducted business with a related party company Anteya Technology Corp. The Company owns 17.33% of the outstanding common stock of Anteya Technology Corp as of June 30, 2015. All transactions were at market-based prices.

Note 14 - Commitments

	Six months ended June 30,	
	2015	2014
Rent expenses	<u>\$37,072</u>	<u>\$24,896</u>

The company leases offices in Taiwan and in California, US under operating leases. Minimum future rental payments due under non-cancelable operating leases with remaining terms at June 30, 2015 are as follows:

2015	<u>29,115</u>
	<u>\$29,115</u>

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COLORSTARS GROUP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 15 - Subsequent Events

The Company evaluated all events subsequent to June 30, 2015 through the date of the issuance of the financial statements, there are no other significant or material transactions to be reported.

