

GIGAMEDIA LTD
Form 20-F
June 30, 2010

Table of Contents

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

FORM 20-F

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2009
Commission File Number: 000-30540**

GIGAMEDIA LIMITED
(Exact name of registrant as specified in its charter)
REPUBLIC OF SINGAPORE
(Jurisdiction of incorporation or organization)
8TH FLOOR, 207 TIDING BOULEVARD, SECTION 2, TAIPEI 114, TAIWAN, R.O.C.
(Address of principal executive offices)
Arthur M. Wang, Chief Executive Officer
8TH FLOOR, 207 TIDING BOULEVARD, SECTION 2, TAIPEI 114, TAIWAN, R.O.C.
Tel: 886-2-2656-8000; Fax: 886-2-2656-8003

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

Title of Each Class	Name of Each Exchange on Which Registered
----------------------------	--

Ordinary Shares	The NASDAQ Stock Market LLC
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Securities registered or to be registered pursuant to Section 12(g) of the Exchange Act:

None

Securities for which there is a reporting obligation 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:

54,994,800 ordinary shares

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 annual report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes No

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP

International Financial Reporting
Standards as issued by the
International Accounting Standards
Board

Other

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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

TABLE OF CONTENTS

	Page
<u>PART I</u>	2
<u>ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS</u>	2
<u>ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE</u>	2
<u>ITEM 3. KEY INFORMATION</u>	2
<u>ITEM 4. INFORMATION ON THE COMPANY</u>	20
<u>ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS</u>	47
<u>ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES</u>	73
<u>ITEM 7. MAJOR SHAREHOLDERS AND RELATED-PARTY TRANSACTIONS</u>	82
<u>ITEM 8. FINANCIAL INFORMATION</u>	83
<u>ITEM 9. THE OFFER AND LISTING</u>	87
<u>ITEM 10. ADDITIONAL INFORMATION</u>	88
<u>ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	97
<u>ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES</u>	98
<u>PART II</u>	98
<u>ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES</u>	98
<u>ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS</u>	99
<u>ITEM 15. CONTROLS AND PROCEDURES</u>	99
<u>ITEM 16. Reserved</u>	100
<u>ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT</u>	100
<u>ITEM 16B. CODE OF ETHICS</u>	100
<u>ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	101
<u>ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES</u>	102
	102

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

ITEM 16F. CHANGES IN REGISTRANT S CERTIFYING ACCOUNTANTS 102

ITEM 16G. CORPORATE GOVERNANCE 102

PART III 102

ITEM 17. FINANCIAL STATEMENTS 102

ITEM 18. FINANCIAL STATEMENTS 103

ITEM 19. EXHIBITS 103

Exhibit 4.34

Exhibit 4.35

Exhibit 4.36

Exhibit 4.37

Exhibit 4.38

Exhibit 4.39

Exhibit 4.40

Exhibit 4.41

Exhibit 4.42

Exhibit 4.43

Exhibit 4.44

Exhibit 8.1

Exhibit 12.1

Exhibit 12.2

Exhibit 13.1

Exhibit 13.2

Exhibit 15.1

Table of Contents

CERTAIN TERMS AND CONVENTIONS

In this annual report, all references to (i) we, us, our, our Company or GigaMedia are to GigaMedia Limited and unless the context requires otherwise, its subsidiaries, or where the context refers to any time prior to the incorporation of any of its subsidiaries, the business which predecessors of the present subsidiaries were engaged in and which were subsequently assumed by such subsidiaries; (ii) Shares are to ordinary shares of our Company; (iii) CESL are to Cambridge Entertainment Software Limited (formerly known as Grand Virtual International Limited), a company incorporated under the laws of The British Virgin Islands; (iv) Hoshin GigaMedia are to Hoshin GigaMedia Center Inc., a company incorporated under the laws of Taiwan, Republic of China, (Taiwan or R.O.C.); (v) FunTown are to our online games business operated through our two operating subsidiaries, Hoshin GigaMedia and FunTown World Limited, a company incorporated under the laws of The British Virgin Islands; (vi) T2CN are to T2CN Holding Limited, a company incorporated under the laws of The British Virgin Islands, and its subsidiaries; (vii) Internet access and service business are to an Internet access and service business that we historically operated through Koos Broadband Telecom Co., Ltd. (KBT) and completely disposed of in September 2008; and (viii) UIM are to Ultra Internet Media S.A., a company incorporated under the laws of Nevis; and (ix) Mangas Everest are to Mangas Everest, a société par actions simplifiée registered with the Trade and Companies Registry of Paris and organized under the laws of France.

For the purpose of this annual report only, geographical references to China and the PRC are to the People's Republic of China and do not include Taiwan, the Hong Kong Special Administrative Region (Hong Kong) and the Macau Special Administrative Region (Macau). Except the context otherwise requires and for the purposes of this annual report only, references to Greater China include the PRC, Taiwan, Hong Kong and Macau. References to South Korea are to the Republic of Korea.

All references in this annual report to U.S. dollar, \$ and US\$ are to the legal currency of the United States; all references to NT dollar or New Taiwan dollar are to the legal currency of Taiwan; all references to RMB, Rmb or Renminbi are to the legal currency of the PRC; and all references to Hong Kong dollar are to the legal currency of Hong Kong.

We have approximated certain numbers in this annual report to their closest round numbers or a given number of decimal places. Due to rounding, figures shown as totals in tables may not be arithmetic aggregations of the figures preceding them.

DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS

This annual report includes forward-looking statements within the meaning of, and intended to qualify for the safe harbor from liability established by, the United States Private Securities Litigation Reform Act of 1995. These statements, which are not statements of historical fact, may contain estimates, assumptions, projections and/or expectations regarding future events, which may or may not occur. These statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Some of the risks are listed under Item 3, Key Information D. Risk Factors and elsewhere in this annual report. In some cases, you can identify these forward-looking statements by words such as anticipate, believe, could, estimate, expect, intend, may, plan, potential, should, will, would, or similar expressions, including These forward-looking statements include, without limitation, statements relating to:

- our business plan and strategies;
- our future business development and potential financial condition, results of operations and other projected financial information;
- our ability to manage current and potential future growth;
- expected continued acceptance of our revenue model;
- our plans for strategic partnerships, licenses and alliances;
- our acquisition and strategic investment strategy, and ability to successfully integrate any past, current, or future acquisitions into our operations;
- our ability to protect our intellectual property rights and the security of our customers' information;
- launch of new online games according to our timetable;

expected continued acceptance of our online games, including expected growth of the online games industry, and consumer preferences for our products and services;

Table of Contents

the in-house development of new online games and our plans to expand our in-house online game development team;

the performance of Mangas Everest and developments in the online gaming industry;

our plans to license additional games from third parties, and the launch of these new games or gaming software systems, including the timing of any such development, licenses or launches, in various geographic markets;

our ability to maintain and strengthen our position as one of the largest online MahJong operators in Taiwan;

our ability to maintain the well-established online sports game platform in the PRC;

potential entry of new competitors in any of our business lines;

changes in the global regulatory environment relating to the online gaming business;

changes or stability in certain regulatory environments relating to Mangas Everest's operations or gaming licenses;

changes in PRC laws and regulations, and future enforcement of those laws and regulations, including laws and regulations relating to Internet usage, advertising over the Internet, Internet content providers, foreign investment and ownership in online business, distribution of dividends and foreign exchange controls;

the outcome of ongoing, or any future, litigation or arbitration; and

our corporate classification by various governmental entities.

These forward-looking statements are based on our own information and on information from other sources we believe to be reliable. Our actual results may differ materially from those expressed or implied by these forward-looking statements as a result of risk factors and other factors noted throughout this annual report, including those described under Item 3, Key Information D. Risk Factors and those detailed from time to time in other filings with the U.S. Securities and Exchange Commission (the SEC). We do not guarantee that the transactions and events described in this annual report will happen as described or that they will happen at all. We undertake no obligation to update or revise any forward-looking statements to reflect events or circumstances after the date of this annual report or to reflect the occurrence of unanticipated events. Whether actual results will conform to our expectations and predictions is subject to a number of risks and uncertainties, many of which are beyond our control, and reflect future business decisions that are subject to change. Given this level of uncertainty, you are advised not to place undue reliance on such forward-looking statements.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable, but see Item 6, Directors, Senior Management and Employees A. Directors and Senior Management in this annual report.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

Exchange Rates

Our consolidated financial statements were historically reported in New Taiwan dollars. Effective January 1, 2004, we adopted the U.S. dollar as our reporting currency because operations denominated in U.S. dollars represented a significant portion of our business following the acquisition of our gaming software and service business. Assets and liabilities on our balance sheet denominated in non-U.S. dollars are translated into U.S. dollars using year-end exchange rates. Income and expense items in our statement of operations denominated in non-U.S. dollars are translated into U.S. dollars using the weighted-average exchange rates. Certain other operating financial information denominated in non-U.S. dollars, not included in our consolidated financial statements and provided in this annual report, are translated using weighted-average exchange rates. For convenience, transactions in 2010 denominated in non-U.S. dollars have been translated into U.S. dollars using the year-end exchange rate for 2009. We make no representation that the non-U.S. dollars could be converted to U.S. dollars at such rate or any particular rates.

Table of Contents**A. Selected Financial Data**

The following selected consolidated balance sheet data as of December 31, 2008 and 2009 and the selected consolidated statement of operations data for the years ended December 31, 2007, 2008 and 2009 have been derived from our audited consolidated financial statements included in Item 18 in this annual report. The selected consolidated balance sheet data as of December 31, 2005, 2006 and 2007, and the selected consolidated statement of operations data for the years ended December 31, 2005 and 2006 have been derived from our audited consolidated financial statements for the years ended December 31, 2005, 2006 and 2007, which are not included in this annual report. The consolidated financial statements have been prepared and presented in accordance with generally accepted accounting principles in the United States, or U.S. GAAP. You should read the following selected consolidated financial data in conjunction with Item 5, Operating and Financial Review and Prospects, and the consolidated financial statements and the accompanying notes to those statements included in this annual report. The statements of operations for the years ended December 31, 2005, 2006, 2007 and 2008 have been retroactively restated to reflect (i) the results of our music distribution business, which was sold in September 2005, and (ii) the results of our Internet access and service business, which was sold in September 2008, as discontinued operations. Certain prior-year amounts have been reclassified to conform to the current-year presentation. These reclassifications had no effect on the results of operations or equity as previously reported.

For the Years Ended December 31,
(in thousands except for earnings per share amounts)

	2005	2006	2007	2008	2009
	US\$	US\$	US\$	US\$	US\$
STATEMENT OF OPERATIONS DATA:					
OPERATING REVENUES					
Gaming software and service revenues	22,511	55,019	118,950	144,765	112,694
Online game and service revenues	0	18,692	32,764	45,604	46,887
Total operating revenues	22,511	73,711	151,714	190,369	159,581
OPERATING COSTS					
Cost of gaming software and service revenues	(3,327)	(7,824)	(16,201)	(22,770)	(20,102)
Cost of online game and service revenues	0	(3,667)	(9,118)	(12,404)	(16,785)
Total operating costs	(3,327)	(11,491)	(25,319)	(35,174)	(36,887)
GROSS PROFIT	19,184	62,220	126,395	155,195	122,694
OPERATING EXPENSES					
Product development and engineering expenses	(2,524)	(5,244)	(7,338)	(13,455)	(14,195)
Selling and marketing expenses	(8,042)	(27,653)	(60,106)	(74,173)	(79,421)
General and administrative expenses	(6,374)	(11,096)	(20,983)	(25,035)	(29,692)
Bad debt expenses	0	(448)	(548)	(2,905)	(1,092)
Impairment loss on property, plant, and equipment	0	0	0	0	(1,250)

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Impairment loss on goodwill	0	0	0	0	(14,103)
Impairment loss on prepaid licensing fees and intangible assets	0	0	0	(1,524)	(23,002)
Total operating expenses	(16,940)	(44,441)	(88,975)	(117,092)	(162,755)
Income (loss) from operations	2,244	17,779	37,420	38,103	(40,061)
Income (loss) from continuing operations	3,525	18,173	39,083	35,710	(56,102)
Income from discontinued operations	2,961	12,932	1,088	9,435	222
Net income (loss)	6,486	31,105	40,171	45,145	(55,880)
Less: Net (income) loss attributable to the noncontrolling interest	(150)	(321)	(1,281)	(757)	6,795
Net income (loss) attributable to GigaMedia	6,336	30,784	38,890	44,388	(49,085)
Earnings (loss) per share (in dollars):					
Basic:					
Income (loss) from continuing operations	0.07	0.35	0.72	0.65	(0.90)
Income from discontinued operations	0.06	0.25	0.02	0.17	0.00
Net income (loss)	0.13	0.60	0.74	0.82	(0.90)
Diluted:					
Income (loss) from continuing operations	0.06	0.30	0.63	0.58	(0.90)
Income from discontinued operations	0.06	0.21	0.02	0.16	0.00
Net income (loss)	0.12	0.51	0.65	0.74	(0.90)

Table of Contents

As of December 31,
(US dollars in thousands except for number of issued shares)

	2005	2006	2007	2008	2009
	US\$	US\$	US\$	US\$	US\$
BALANCE SHEET DATA:					
Total current assets	70,204	64,176	115,417	128,799	104,839
Property, plant and equipment-net	10,747	10,098	13,008	13,468	5,989
Goodwill	29,243	55,817	85,149	87,098	44,417
Intangible assets-net	2,704	23,067	26,060	28,930	18,924
Total assets	113,519	182,619	283,865	316,793	260,181
Total GigaMedia shareholders' equity	100,648	134,087	180,665	228,456	184,745
Common shares, no par value, and additional paid-in capital	287,920	289,495	296,793	300,021	304,379
Number of issued shares (in thousands)	50,344	51,495	53,700	54,365	54,995
Dividends declared per share (in dollars)	0	0	0	0	0

Presentation of financial information for the years ended December 31, 2005, 2006, 2007 and 2008 has been reclassified to conform to the presentation for the year ended December 31, 2009 for non-controlling interest.

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors**Risks Related to Our Business and Industries****The limited operating history of the Mangas Everest business and our online games business may not provide you with an adequate basis upon which to evaluate our business and prospects**

We commenced our gaming software and service business operations in April 2004 and our online games business in January 2006. We sold 60 percent interest in our gaming software business to Mangas Gaming (Mangas), a leading European sports betting and online gaming group, on April 8, 2010. The strategic alliance with Mangas was structured as a stock and asset sale to a newly-formed French entity, Mangas Everest, in which we hold a 40 percent stake.

Mangas Everest's operating history as an online gambling operator and our operating history as an online games operator may be too short to give you a sufficient basis for evaluating our business and financial performance. It is also difficult to evaluate our prospective business, because we may not have sufficient experience to address the risks frequently encountered by companies entering new and rapidly evolving markets such as the online gaming and online games market. These risks include our potential failure to:

- respond to technological changes or resolve unexpected service interruptions in a timely manner;
- adapt to regulatory changes;
- retain existing customers or attract new customers;

Table of Contents

license, develop, or acquire additional online games that are appealing to consumers;
anticipate and adapt to changing consumer preferences;
adapt to competitive market conditions;
adequately and efficiently operate, upgrade and develop our transaction and service platforms; and
maintain adequate control of our expenses.

If we are unsuccessful in addressing any of these risks, our business and financial condition will be adversely affected. In addition, certain management members have worked at our Company for a relatively short period. We may not be able to achieve similar results or growth in future periods. Accordingly, you should not rely on our results of operations for any prior periods as an indication of our future performance.

In operating our online games business, we may fail to launch new games according to our timetable, and our new games may not be commercially successful

In order for our online games business strategy to succeed over time, we will need to license, acquire or develop new online games that can generate additional revenue and further diversify our revenue sources. A number of factors, including technical difficulties, government approvals and game licenses required for launching new games, lack of sufficient game development personnel and other resources, and adverse developments in our relationship with the licensors of our new licensed games could result in delay in launching our new games. Therefore, we cannot assure you that we will be able to meet our timetable for new game launches.

In January 2009, we introduced Holic Online, an adventure-themed massively multi-player online role playing game (MMORPG), in Taiwan. On June 25, 2009, we launched Warhammer Online: Age of Reckoning, a war-themed MMORPG, in Taiwan, Hong Kong and Macau. On July 7, 2009, we launched Luna Online, a casual fantasy-themed MMORPG in the PRC. Warhammer Online: Age of Reckoning and Luna Online were not commercially successful in the territories in which they were launched. As a result, we terminated the license agreements for these two games in April 2010 and June 2010, respectively. In addition, we have one MMORPG and two advanced casual games in the pipeline, which we expect to launch in various target markets in Greater China, including the PRC, Taiwan, Hong Kong and Macau. There are many factors that may adversely affect the popularity of our new games. For example, we may fail to anticipate and adapt to future technical trends and new business models, fail to satisfy game player preferences and requirements, fail to effectively plan and organize marketing and promotion activities, fail to effectively detect and prevent programming errors or defects in the games, and fail to operate our new games at acceptable costs. We cannot assure you that our new games will gain market acceptance and become commercially successful. If we are not able to license, develop or acquire additional online games that are commercially successful, our future revenues and profitability may decline.

Due to increased competition among online games operators in the PRC and Taiwan, license fees for online games have increased and most licensors are demanding upfront license fees and guaranteed minimum royalty payments. If any of the new games we license from third parties fails to appeal to players, we may not be able to fully recover upfront and/or minimum royalty licensing costs, which can be significant. As a result, our results of operations and financial condition may be materially and adversely affected.

We may not be successful in operating and improving our existing online games to satisfy the changing demands and preferences of players

The level of demand and market acceptance of our existing online games is subject to a high degree of uncertainty. Our future operating results will depend on numerous factors, many of which are beyond our control. These factors include:

the popularity of existing and new online games operated by us;
the introduction of new online games by us or third parties, competing with or replacing our existing online games;
general economic conditions, particularly economic conditions adversely affecting discretionary consumer spending;
changes in our customer demands and preferences;
the availability of other forms of entertainment; and
critical reviews and public tastes and preferences, all of which change rapidly and cannot be predicted.

Table of Contents

Our ability to plan for product development and distribution and promotional activities will be significantly affected by how well we anticipate and adapt to relatively rapid changes in consumer tastes and preferences. Currently, a substantial portion of our online games revenue is derived from revenues from Freestyle, an online sports game offered in the PRC, and the online MahJong games offered in Taiwan and Hong Kong. However, there is no assurance that these games will continue to be popular. A decline in the popularity of online games in general or, in particular, Freestyle and online MahJong, is likely to adversely affect our business, financial condition and results of operations. To maintain competitiveness of our games, we are generally required to continuously invest in enhancing, improving, expanding or upgrading our games. If we fail to do so, revenues generated from our existing games may decline. In addition, we expect that as we introduce new online games, a portion of our existing customers will switch to the new games. If this transfer of players from our existing games exceeds our expectations, we may have to adjust our marketing, pricing and other business plans and, as a result, our growth and profitability could be materially and adversely affected.

Our results of operations are subject to significant fluctuations

Our revenues, expenses and results of operations have varied in the past and may fluctuate significantly in the future due to a variety of factors, many of which are beyond our control. The key factors affecting our businesses include:

Gaming software and service business: the regulatory restrictions applicable to the Internet gaming industry; the revenues, expenses and results of operations of Mangas Everest, our joint venture with Mangas; global economic conditions and general economic conditions of the markets where our products target; availability of the Internet infrastructure; and the technological and other competition from existing and new competitors.

Online games business: our ability to retain existing users; attract new users and maintain user satisfaction; the pace of rolling out new games or updating existing games by us or our competitors; the amount and timing of operating costs and capital expenditures relating to our business operations and expansion; seasonal trends in Internet use; price competition in the industry; regulatory and other risks associated from our operations in China and Taiwan.

In addition, our operating expenses are based on our expectations of the future demand for our services and are relatively fixed in the short term. We may be unable to adjust spending quickly enough to offset any unexpected demand shortfall. A decrease in revenues in relation to our expenses could have a material and adverse effect on our business, results of operations and financial condition. You should not place undue reliance on our financial guidance, nor should you rely on year-to-year or quarter-to-quarter comparisons of our results of operations as indicators of our future performance.

The online games market is characterized by rapid technological change, and failure to respond quickly and effectively to new Internet technologies or standards may have a material adverse effect on our business

The online games industry is evolving rapidly. Any new technologies and new standards may require increases in expenditures for online game development and operations. In addition, we use internally developed software systems that support nearly all aspects of our billing and payment transactions in our online games business. All of our businesses may be adversely affected if we are unable to upgrade our systems effectively to accommodate future traffic levels, to avoid obsolescence or to successfully integrate any newly developed or acquired technology with our existing systems. Capacity constraints could cause unanticipated system disruptions and slower responses, which could adversely affect data transmission and game play. These factors could, among other things, cause us to lose existing or potential users and existing or potential game development partners.

The current global economic slowdown and other adverse economic conditions may negatively impact our business

The current global economic slowdown has resulted in an increased level of commercial and consumer delinquencies, lack of consumer confidence and increased market volatility. These unfavorable changes in economic conditions have resulted in decreased spending by our customers. The impact of economic conditions on our licensees and business partners could adversely affect our business and revenues. In addition, the current global financial turmoil and the tightening of credit have resulted in a general credit crunch and have negatively impacted our ability to obtain additional financings. If the current global economic slowdown and global financial turmoil continue on a sustained

basis, they will further negatively impact the demand for our online games and Mangas Everest's gaming software products and services and adversely affect our business, revenues, cash flows, profitability and financial condition.

Table of Contents**Our business could suffer if we do not successfully manage current growth and potential future growth**

We are pursuing a number of growth strategies. Some of these strategies relate to services, products or markets in which we lack experience and expertise. As part of our growth strategy for the online games operation, in December 2006, we entered into a strategic alliance with Infocomm Asia Holdings Pte Ltd (Infocomm Asia), an online gaming operator and distributor operating primarily in the Southeast Asia region, in which we had no business operations at that time. On April 30, 2010, we increased our investment in Infocomm Asia by acquiring additional preferred shares from Infocomm Asia and certain shareholders of Infocomm Asia. The acquisition of Infocomm Asia is expected to close in the third quarter of 2010 and upon closing, we will hold preferred shares convertible into approximately 80 percent of the common shares of Infocomm Asia. Infocomm Asia has entered into certain license agreements with Blizzard Entertainment International, a division of Coöperatie Activision Blizzard International U.A. (Blizzard), under which Blizzard agreed to license certain games to Infocomm Asia or its wholly owned subsidiary in Southeastern Asia. We cannot assure you that we will be able to leverage our past experience and successfully manage our expansion into Southeastern Asia and other new markets.

Our growth to date has placed, and our anticipated further expansion of our operations will continue to place, a significant strain on our management, operation systems and resources. In addition to training and managing our workforce, we will need to continue to develop and improve our financial and management controls and our reporting systems and procedures, including those of acquired businesses. We cannot assure you that we will be able to effectively manage the growth of our operations, and any failure to do so may limit our future growth and materially and adversely affect our business, financial condition and results of operations.

Our business strategy, which contemplates growth through acquisitions and strategic investments, exposes us to significant risks

We have pursued and may continue to pursue growth through acquisitions and strategic investments. Any acquisition or investment is subject to a number of risks. Such risks include the diversion of management time and resources, disruption of our ongoing business, lack of familiarity with new markets, difficulties in supporting the acquired business, and dilution to existing stockholders if our common stock is issued in consideration for an acquisition or investment, incurring or assuming indebtedness or other liabilities in connection with an acquisition.

The total costs incurred in connection with our acquisitions and investments in various businesses in 2009 were approximately US\$9.9 million. For additional information with respect to our acquisitions and investments, see Item 4, Information on The Company A. History and Development of Our Company in this annual report. Our financial results may be affected by such acquisitions or investments. We may incur debts upon an acquisition or suffer losses related to the impairment of goodwill and other intangible assets following the acquisition. These debts or losses could negatively impact our results of operations. We recognized impairment loss on goodwill of approximately US\$14.1 million and impairment loss on marketable securities and investments of approximately US\$15.7 million in 2009. (See note 10 Marketable Securities Current to our consolidated financial statements for additional information). Any impairment on goodwill and marketable securities and investments in the future will have a negative impact on our financial results.

We will continue to examine the merits, risks and feasibility of potential transactions, and expect to explore additional acquisition opportunities in the future. Such examination and exploration efforts, and any related discussions with third parties, may or may not lead to future acquisitions and investments. We may not be able to complete acquiring or investing transactions that we initiate. Our ability to grow through such acquisitions and investments will depend on many factors, including the availability of suitable acquisition candidates at an acceptable cost, our ability to reach agreement with acquisition candidates or investee companies on commercially reasonable terms, the availability of financing to complete the transactions and our ability to obtain any required governmental approvals.

We also face challenges in integrating any acquired business. These challenges include eliminating redundant operations, facilities and systems, coordinating management and personnel, retaining key employees, managing different corporate cultures, maintaining the relationship with the suppliers, vendors and/or distributors of acquired businesses, and achieving cost reductions and cross-selling opportunities. There can be no assurance that we will be able to successfully integrate all aspects of acquired businesses. The process of integrating the acquired business may disrupt our business and divert our resources. In addition, the benefits of an acquisition or investment transaction may

take considerable time to be fully realized and we cannot assure you that any particular acquisition or investment and the subsequent integration will produce the intended benefits.

Our online games business faces intense competition, which may adversely affect our revenues, profitability and planned business expansion

The online games market is highly competitive. Our main competitors in the online games business are online game operators in Taiwan and China. Our major competitors in Taiwan include Gamania Digital Entertainment Co., Ltd. (Gamania), Soft-World International Corporation (Soft-World), International Games System, Co., Ltd. (IGS), UserJoy Technology Co., Ltd. (UserJoy) and GodGame Inc. (GodGame). Our major competitors in the PRC include Shanda Interactive Entertainment Ltd. (Shanda), Giant Interactive Group, Inc. (Giant), Changyou.com Limited (Changyou), The9 Limited, Shanghai Everstar Online Entertainment Co., Ltd. (Nineyou), Tencent Holdings Limited (Tencent), Beijing Globalink Computer Technology Co., Ltd.(Ourgames.com) and Chinagames.net.

Table of Contents

In addition, we compete for users against various offline games, such as console games, arcade games and handheld games, as well as various other forms of traditional or online entertainment.

We expect more online games operating companies to enter in the markets where we operate, including Taiwan, the PRC and Hong Kong, and a wider range of online games to be introduced to these markets, given the relatively low entry barriers to the online games industry. Our competitors vary in size and include private and public companies, many of which have greater financial, marketing and technical resources as well as name recognition. We intend to continue to enhance our market position through providing competitive products and quality services that meet market trends and users' preferences, as well as strengthening sales effectiveness.

As a result of the above, significant competition may reduce the number of our users or the growth rate of our user base, reduce the average number of hours played by our users, or cause us to reduce usage fees. All of these competitive factors could have a material adverse effect on our business, financial condition and results of operations.

Our online games business depends on the reliability of the network infrastructure and related services provided by ourselves and third parties, which is subject to physical, technological, security and other risks; the Mangas Everest business also faces similar risks

The development and operation of our online networks and those of Mangas Everest, are subject to physical, technological, security and other risks which may result in interruption in service or reduced capacity. These risks include physical damage, power loss, telecommunications failure, capacity limitation, hardware or software failures or defects and breaches of security by computer viruses, system break-ins or otherwise. An increase in the volume of usage of online services could strain the capacity of the software and hardware employed, which could result in slower response time or system failures. We have a variety of backup servers at our primary site to deal with possible system failures. However, we do not have redundant facilities in the event of an emergency. The occurrence of any of these events could result in interruptions, delays or cessation in service to users of our online services, which could have a material adverse effect on our business and results of operations.

While we and Mangas Everest have implemented industry-standard security measures, our network and those of Mangas Everest may still be vulnerable to unauthorized access, computer viruses, denial of service and other disruptive problems. Our Internet-based services may be interrupted as a result of the accidental or intentional actions of Internet users, our current and former employees or others. A party that is able to circumvent security measures could misappropriate proprietary information, attack our security and network system, and, perhaps, most importantly, cause interruptions in our operations. We and Mangas Everest have experienced, in the past, and may experience, in the future, security breaches and attacks. We may be required to expend significant capital or other resources to protect against the threat of security breaches and attacks or to alleviate problems caused by such actions. There can be no assurance that any measures implemented will not be circumvented in the future.

Our business and that of Mangas Everest are also vulnerable to delays or interruptions due to our reliance on infrastructure and related services provided by third parties. End-users of Mangas Everest's gaming software depend on ISPs and Mangas Everest's system infrastructure for access to the Internet gaming sites operated by UIM and its sub-licensees and currently by Mangas Everest. Many of these services have experienced service outages in the past and could experience service outages, delays and other difficulties due to system failures, stability or interruption. For example, in February 2007, an earthquake off the coast of Taiwan damaged several undersea fiber optic cables linking countries such as Malaysia, Singapore, Australia, Japan, South Korea, China, the United States and Europe, causing disruptions in Internet traffic worldwide. We may lose customers as a result of delays or interruption in service, including delays or interruptions relating to high volumes of traffic or technological