

GIGAMEDIA LTD
Form 20-F
June 30, 2011

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, 2010
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)
Yichin LEE, 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

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:

56,262,575 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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant (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

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>	3
<u>ITEM 4. INFORMATION ON THE COMPANY</u>	22
<u>ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS</u>	56
<u>ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES</u>	87
<u>ITEM 7. MAJOR SHAREHOLDERS AND RELATED-PARTY TRANSACTIONS</u>	96
<u>ITEM 8. FINANCIAL INFORMATION</u>	98
<u>ITEM 9. THE OFFER AND LISTING</u>	105
<u>ITEM 10. ADDITIONAL INFORMATION</u>	107
<u>ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	117
<u>ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES</u>	118
<u>PART II</u>	118
<u>ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES</u>	118
<u>ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS</u>	119
<u>ITEM 15. CONTROLS AND PROCEDURES</u>	120
<u>ITEM 16. RESERVED</u>	122
<u>ITEM 16 A. AUDIT COMMITTEE FINANCIAL EXPERT</u>	122
<u>ITEM 16 B. CODE OF ETHICS</u>	122
<u>ITEM 16 C. PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	122
<u>ITEM 16 D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES</u>	123

<u>ITEM 16 E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS</u>	123
<u>ITEM 16 F. CHANGES IN REGISTRANT S CERTIFYING ACCOUNTANTS</u>	123
<u>ITEM 16 G. CORPORATE GOVERNANCE</u>	124
<u>PART III</u>	124
<u>ITEM 17. FINANCIAL STATEMENTS</u>	124
<u>ITEM 18. FINANCIAL STATEMENTS</u>	124
<u>ITEM 19. EXHIBITS</u>	124
<u>Exhibit 4.45</u>	
<u>Exhibit 4.46</u>	
<u>Exhibit 4.47</u>	
<u>Exhibit 4.48</u>	
<u>Exhibit 4.49</u>	
<u>Exhibit 4.50</u>	
<u>Exhibit 4.51</u>	
<u>Exhibit 4.52</u>	
<u>Exhibit 4.53</u>	
<u>Exhibit 8.1</u>	
<u>Exhibit 12.1</u>	
<u>Exhibit 12.2</u>	
<u>Exhibit 13.1</u>	
<u>Exhibit 13.2</u>	
<u>Exhibit 15.1</u>	
<u>Exhibit 15.2</u>	
<u>Exhibit 15.3</u>	
<u>Exhibit 18.1</u>	
<u>Exhibit 18.2</u>	

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 Asian online game and service 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 T2CN Operating Entities; (vii) T2CN Operating Entities are to T2CN Holding Limited's two wholly owned subsidiaries, T2CN Information Technology (Shanghai) Co., Ltd. (T2 Technology) and J-Town Information (Shanghai) Co., Ltd. (J-Town), and three variable interest entities, Shanghai T2 Entertainment Co., Ltd. (T2 Entertainment), Shanghai T2 Advertisement Co., Ltd. (T2 Advertisement) and Shanghai Jinyou Network & Technology Co., Ltd. (Jinyou); (viii)

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 (ix) UIM are to Ultra Internet Media S.A., a company incorporated under the laws of Nevis; (xi) Everest Gaming are to Mangas Everest S.A.S, a société par actions simplifiée registered with the Trade and Companies Registry of Paris and organized under the laws of France; (xii) BetClic are to BetClic Everest Group, formerly named as Mangas Gaming S.A.S, a company organized under the laws of France. BetClic, owned equally by Lov Group and La Société des Bains de Mer, is one of the leaders in the online gaming industry and has a unique portfolio comprising four diverse and complementary international brands, Everest Gaming, BetClic, bet-at-home.com and Expekt; (xiii) IAHGames are to Infocomm Asia Holdings Pte. Ltd., an online game operator, publisher and distributor in Southeast Asia and incorporated under the laws of the Republic of Singapore; (xiv) Monsoon are to Monsoon Online Pte. Ltd., a company incorporated under the laws of the Republic of Singapore and wholly owned by IAHGames; (xv) JIDI are to JIDI Network Technology (Shanghai) Co., Ltd., our wholly owned subsidiary incorporated under the laws of the PRC; and (xvi) Shanghai JIDI are to Shanghai JIDI Network Technology Co., Ltd., a company incorporated under the laws of the PRC.

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 if 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; all references to Hong Kong dollar are to the legal currency of Hong Kong and all references to Singapore dollar and S\$ are to the legal currency of the Republic of Singapore. 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;

Table of Contents

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;
the 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;
the in-house development of new online games and our plans to expand our in-house online game development team;
the performance of Everest Gaming 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;
the 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 Everest Gaming'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.

Table of Contents**ITEM 3. KEY INFORMATION****Exchange Rates**

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 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 2011 denominated in non-U.S. dollars have been translated into U.S. dollars using the year-end exchange rate for 2010. We make no representation that the non-U.S. dollars could be converted to U.S. dollars at such rate or any particular rates.

A. Selected Financial Data

The following selected consolidated balance sheet data as of December 31, 2009 and 2010 and the selected consolidated statement of operations data for the years ended December 31, 2008, 2009 and 2010 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, 2006, 2007 and 2008, and the selected consolidated statement of operations data for the years ended December 31, 2006 and 2007 have been derived from our audited consolidated financial statements for the years ended December 31, 2006, 2007 and 2008, 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, 2006, 2007, and 2008 have been restated to reflect 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 shareholders' equity as previously reported.

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

	2006	2007	2008	2009	2010
	US\$	US\$	US\$	US\$	US\$
STATEMENT OF OPERATIONS					
DATA:					
OPERATING REVENUES					
Gaming software and service revenues	55,019	118,950	144,765	112,694	25,820
Asian online game and service revenues	18,692	32,764	45,604	46,887	38,862
Total operating revenues	73,711	151,714	190,369	159,581	64,682
OPERATING COSTS					
Cost of gaming software and service revenues	(7,824)	(16,201)	(22,770)	(20,102)	(4,010)
Cost of Asian online game and service revenues	(3,667)	(9,118)	(12,404)	(16,785)	(17,103)
Total operating costs	(11,491)	(25,319)	(35,174)	(36,887)	(21,113)
GROSS PROFIT	62,220	126,395	155,195	122,694	43,569

OPERATING EXPENSES

Product development and engineering expenses	(5,244)	(7,338)	(13,455)	(14,195)	(7,301)
Selling and marketing expenses	(27,653)	(60,106)	(74,173)	(79,421)	(21,589)
General and administrative expenses	(11,096)	(20,983)	(25,035)	(29,692)	(31,780)
Bad debt expenses	(448)	(548)	(2,905)	(1,092)	(1,639)
Impairment loss on property, plant, and equipment	0	0	0	(1,250)	(278)
Impairment loss on goodwill	0	0	0	(14,103)	(2,255)
Impairment loss on prepaid licensing fees and intangible assets	0	0	(1,524)	(23,002)	(2,200)
Impairment loss on deconsolidation of T2CN	0	0	0	0	(22,234)
Other	0	0	0	0	(1,989)
Total operating expenses	(44,441)	(88,975)	(117,092)	(162,755)	(91,265)
Income (loss) from operations	17,779	37,420	38,103	(40,061)	(47,696)
Income (loss) from continuing operations	18,173	39,083	35,710	(56,102)	1,408
Income (loss) from discontinued operations	12,932	1,088	9,435	222	(128)
Net income (loss)	31,105	40,171	45,145	(55,880)	1,280

Table of Contents

	2006	2007	2008	2009	2010
	US\$	US\$	US\$	US\$	US\$
Less: Net (income) loss attributable to the noncontrolling interest and subsidiary preferred shares	(321)	(1,281)	(757)	6,795	1,370
Net income (loss) attributable to GigaMedia	30,784	38,890	44,388	(49,085)	2,650
Earnings (loss) per share (in dollars):					
Basic:					
Income (loss) from continuing operations	0.35	0.72	0.65	(0.90)	0.05
Income (loss) from discontinued operations	0.25	0.02	0.17	0.00	0.00
Net income (loss)	0.60	0.74	0.82	(0.90)	0.05
Diluted:					
Income (loss) from continuing operations	0.30	0.63	0.58	(0.90)	0.04
Income (loss) from discontinued operations	0.21	0.02	0.16	0.00	0.00
Net income (loss)	0.51	0.65	0.74	(0.90)	0.04

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

	2006	2007	2008	2009	2010
	US\$	US\$	US\$	US\$	US\$
BALANCE SHEET DATA:					
Total current assets	64,176	115,417	128,799	104,839	93,088
Property, plant and equipment-net	10,098	13,008	13,468	5,989	5,301
Goodwill	55,817	85,149	87,098	44,417	39,493
Intangible assets-net	23,067	26,060	28,930	18,924	19,769
Total assets	182,619	283,865	316,793	260,181	267,589
Total GigaMedia's shareholders equity	134,087	180,655	228,456	184,745	217,521
Common shares, no par value, and additional paid-in capital	289,495	296,793	300,021	304,379	309,332
Number of issued shares (in thousands)	51,495	53,700	54,365	54,995	56,263
Dividends declared per share (in dollars)	0	0	0	0	0

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

Table of Contents**D. Risk Factors****Risks Related to Our Business and Industries****The limited operating history of the Everest Gaming business and our Asian online game and service 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 Asian online game and service business in January 2006. We sold 60 percent interest in our gaming software business to BetClic, a leading European sports betting and online gaming group, on April 8, 2010. The strategic alliance with BetClic was structured as a stock and asset sale to a newly-formed French entity, Everest Gaming, in which we hold a 40 percent stake. Everest Gaming'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;
- 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. 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 Asian online game and service 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 Asian online game and service 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. Holic Online was not commercially successful in Taiwan. As a result, we terminated the Holic Online exclusive game license agreement in December 2010 and completely ceased the operation in March 2011. 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 three MMORPGs and two advanced casual games non-role playing massively multiplayer online games (non-RPG MMOs) in the pipeline, which we expect to launch in various target markets in Greater China. 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, Taiwan and Southeast Asia, 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.

Table of Contents**We may not be able to maintain a stable relationship with Blizzard, and we may experience difficulties in the operation of the online games licensed from Blizzard**

Monsoon, a wholly owned subsidiary of IAHGames in which we are a controlling shareholder, entered into various agreements with Blizzard Entertainment International, a division of Coöperatie Activision Blizzard International U.A. (Blizzard) to distribute selected Blizzard Entertainment games in Singapore, Malaysia, Thailand, Indonesia and the Philippines. The license and distribution agreements include bestselling games from Blizzard s Diablo® action-role-playing-game series, Warcraft® and StarCraft® real-time strategy-game series, including StarCraft II: Wings of Liberty , and World of Warcraft and its three expansion sets, The Burning Crusade®, Wrath of the Lich King® and Cataclysm . We have guaranteed to Blizzard the due and punctual observance by each of Monsoon and IAHGames of all of its respective financial obligations under various license and distribution agreements and services agreements and agreed to pay to Blizzard from time to time on demand by Blizzard all sums of money which either Monsoon and/or IAHGames is liable to pay to Blizzard under those agreements. Blizzard has the right to terminate those license and distribution agreements or services agreements under certain circumstances. See Item 4.B. Business Overview Asian Online Game and Service Business Our Operating Entities IAHGames.

We have limited experience working with Blizzard. If we are unable to maintain a stable relationship with Blizzard, or if Blizzard either establishes similar or more favorable relationships with our competitors in violation of its contractual arrangements with us or otherwise, we may not be able to ensure smooth operation of these licensed online games, and Blizzard could terminate the license and distribution agreements and services agreements with us, which could adversely affect our business, financial condition and results of operations. Also, the benefits of our arrangements with Blizzard may take considerable time to develop, and we cannot be certain that such arrangements will produce its intended benefits. We cannot assure you that we will be able to leverage our past experience and successfully manage our expansion into Southeast Asia markets.

In addition, we cannot be certain that these licensed online games will be viewed by the applicable regulatory authorities as complying with content restrictions, will be launched or distributed as scheduled, or at all, will be attractive to game players or will be able to compete with games operated by our competitors. We may not be able to fully recover the costs associated with licensing these licensed games if these games are not popular among game players, and any difficulties in the operation or distribution of these licensed games could adversely affect our business, financial condition and results of operations.

Due to our ongoing dispute with the former chief executive officer of T2CN, we have lost effective control over the T2CN Operating Entities and we may not be able to regain effective control over the T2CN Operating Entities or T2CN s assets

Due to our dispute with Wang Ji, the former head of our Asian online game and service business in the PRC and former chief executive officer of T2CN, that arose in July 2010, we have lost effective control over a majority of T2CN s assets and its financial reporting process since July 1, 2010.

We believe that Wang Ji currently has in his possession, among other things, the company seals, financial chops and business registration certificates of the T2CN Operating Entities. We also believe that Wang Ji has in his possession all documents, records and data and tangible property, including license agreements, trademark and domain name documentation, held in the offices of the T2CN Operating Entities. The company seals, financial chops and business registration certificates of the T2CN Operating Entities are necessary for the respective entities to, among other things, declare dividends and approve service fee payments to us. These documents are necessary for us to run our Asian online game and service business in the PRC. Under PRC law, the company seals, financial chops and business registration certificates are essential for entering into contracts, conducting banking business, or taking official corporate action of any sort including registering any change to the composition of the board or management with the relevant PRC authorities.

Consequently, we have not been able to register the resolutions removing Wang Ji from his position as a director of T2 Technology and J-Town and as the legal representative, executive director and manager of T2 Entertainment. As a result, Wang Ji has effectively usurped control over T2 Technology, J-Town and T2 Entertainment s operations and accounts.

We have been seeking to regain effective control over T2CN and its assets by a range of means, including pursuing legal remedies in the courts of the PRC, Hong Kong, Singapore and the British Virgin Islands. While we continue to pursue these actions, we have to date not been successful in regaining control of T2CN or recovering its assets. We deconsolidated T2CN's financial results with effect from July 1, 2010 and wrote off our investment and advances to the entities held or controlled by T2CN (amounting to US\$23.6 million, including the recorded investment of \$22.2 million and advances of approximately \$1.4 million) in the fourth quarter of 2010. While we will continue pursue legal remedies, we may also seek to reach a settlement with Wang Ji.

If our efforts to regain control over T2CN or its assets are unsuccessful, our future results of operations will likely be harmed. Our loss of control over T2CN and efforts to regain control also continues to occupy significant management time and resources. Moreover, our efforts to regain control over T2CN could hamper future business development efforts in China.

See Item 8, Financial Information A. Consolidated Statements and Other Financial Information Information on Legal or Arbitration Proceedings Dispute with the former head of our Asian online game and service business in the PRC and former Chief Executive Officer of T2CN in this annual report.

Table of Contents**Failure to maintain effective internal controls could have a material adverse effect on our business, results of operations and the trading price of our Shares**

Effective internal controls are necessary for us to provide reasonable assurance with respect to our financial reports and to effectively prevent fraud. If we cannot provide reasonable assurance with respect to our financial reports and effectively prevent fraud, our results of operations could be materially and adversely affected. We are subject to reporting requirements under the U.S. securities laws. The SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, has adopted rules requiring public companies to include a report of management on such company's internal control over financial reporting in its annual report, which must contain an assessment by management of the effectiveness of such company's internal control over financial reporting. In making such assessment, our management also used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework. In addition, an independent registered public accounting firm must express an opinion on the effectiveness of our Company's internal control over financial reporting.

Our management conducted an evaluation of the effectiveness of our internal control over financial reporting and concluded that as of December 31, 2010, our disclosure controls and procedures were not effective at a reasonable assurance level in that they failed to timely detect the circumvention of our internal controls and procedures which resulted in our inability to exercise sufficient control over a majority of T2CN's assets and its financial reporting process. We excluded IAHGames from our assessment of internal control over financial reporting as of December 31, 2010 because we acquired a controlling financial interest in the assets underlying the business of IAHGames and began to consolidate this business on July 1, 2010, which qualified under current SEC interpretive guidance for exclusion from our assessment of internal control over financial reporting. Since early July 2010 when the Company started to implement the internal restructuring plan with respect to T2CN's leadership team, there have been disputes between the Company and the former chief executive officer of T2CN over his future role in the Company and T2CN. Due to these disputes, the former chief executive officer of T2CN effectively usurped control over and access to the accounts of the T2CN Operating Entities, and has taken actions or directed subordinates to take actions that circumvented the existing internal control system. As a result, we determined that there were inadequate controls in place to address risks related to usurpation of established policies, procedures and control systems related to T2CN which resulted in our inability to exercise sufficient control over a majority of T2CN's assets and its financial reporting process, which eventually resulted in a significant loss to the Company. Our management believes that our loss of and continuing inability to maintain sufficient control over a majority of T2CN's assets and its financial reporting process has been mainly caused by the actions of the former chief executive officer of T2CN as described above. As a result of this loss of control, in the fourth quarter of 2010, we recorded a full impairment of \$22.2 million against our remaining investment in T2CN and we have recognized a full provision against the loan of \$1.4 million due from T2CN. Our management does not believe that the material weakness described above has caused our financial statements as of and for the year ended December 31, 2010 to contain a material misstatement, as management completely impaired both the Company's investment in and advances to T2CN during the fourth quarter of 2010 in order to properly reflect the Company's financial position as of December 31, 2010.

We have completed our Section 404 assessment under the Sarbanes-Oxley Act and received our auditors' attestation as of December 31, 2010. The report of our independent registered public accounting firm includes an opinion regarding the effectiveness of our internal control over financial reporting. However, internal control over financial reporting may not prevent or detect misstatements because of its inherent limitations, including the possibility of human error, the circumvention or overriding of controls, or fraud. Therefore, even effective internal controls can provide only reasonable assurance with respect to the preparation and fair presentation of financial statements. In addition, projections of any evaluation of effectiveness of internal control over financial reporting to future periods are subject to the risk that the control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our failure to maintain effective internal control over financial reporting could result in the loss of investor confidence in the reliability of our financial statements, which in turn could harm our business and negatively impact the trading price of our Shares. Furthermore, we may incur additional costs and use significant management and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act going forward.

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;

Table of Contents

changes in our customer demands and preferences;
regulatory and other risks associated with our operations in China, Taiwan and Southeast Asia;
the availability of other forms of entertainment; and
critical reviews and public tastes and preferences, all of which change rapidly and cannot be predicted.
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 reven