ChinaNet Online Holdings, Inc.
Form 10-Q
May 20, 2013

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

FORM 10-Q

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2013

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____ to _____

Commission File Number: 001-34647

ChinaNet Online Holdings, Inc.
(Exact name of registrant as specified in its charter)

Nevada	20-4672080
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

No. 3 Min Zhuang Road, Building 6,
Yu Quan Hui Gu Tuspark, Haidian District, Beijing, PRC 100195
(Address of principal executive offices) (Zip Code)

+86-10-5160-0828
(Registrant's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check 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 [x] 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 [x] No [ ]

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

Large accelerated filer [ ]   Accelerated filer [ ]   Non-accelerated filer (Do not check if a smaller reporting company) [ ]   Smaller reporting company [x]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes [ ] No [x]

As of May 20, 2013 the registrant had 22,186,540 shares of common stock outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Interim Financial Statements

CHINANET ONLINE HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands)

	March 31, 2013 (US $) (Unaudited)	December 31, 2012 (US $)
Assets		
Current assets:		
Cash and cash equivalents	$ 3,792	$ 5,483
Term deposit	3,375	3,357
Accounts receivable, net	9,831	8,486
Other receivables, net	3,128	3,103
Prepayment and deposit to suppliers	14,822	14,596
Due from related parties	260	210
Other current assets	135	136
Deferred tax assets-current	42	50
Total current assets	35,385	35,421
Investment in and advance to equity investment affiliates	892	959
Property and equipment, net	1,501	1,636
Intangible assets, net	6,944	7,167
Goodwill	11,144	11,083
Deferred tax assets-non current	794	652
Total Assets	$ 56,660	$ 56,918
Liabilities and Equity		
Current liabilities:		
Accounts payable *	$ 219	$ 110
Advances from customers *	1,636	1,065
Accrued payroll and other accruals *	877	904
Payable for acquisition *	-	1,266
Taxes payable *	6,846	6,683
Other payables *	240	217
Total current liabilities	9,818	10,245

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CHINANET ONLINE HOLDINGS, INC.
CONSOLIDATED BALANCE SHEETS (CONTINUED)
(In thousands, except for number of shares and per share data)

	March 31, 2013 (US $) (Unaudited)	December 31, 2012 (US $)
Long-term liabilities:		
Deferred tax liability-non current *	1,643	1,689
Long-term borrowing from director	139	139
Total Liabilities	11,600	12,073
Commitments and contingencies		
Equity:		
ChinaNet Online Holdings, Inc.'s stockholders' equity		
Common stock (US$0.001 par value; authorized 50,000,000 shares; issued and outstanding 22,186,540 shares at March 31, 2013 and December 31, 2012)	22	22
Additional paid-in capital	20,019	20,008
Statutory reserves	2,296	2,296
Retained earnings	19,535	19,505
Accumulated other comprehensive income	2,605	2,393
Total ChinaNet Online Holdings, Inc.'s stockholders' equity	44,477	44,224
Noncontrolling interests	583	621
Total equity	45,060	44,845
Total Liabilities and Equity	$ 56,660	$ 56,918

*All of the VIEs' assets can be used to settle obligations of their primary beneficiary. Liabilities recognized as a result of consolidating these VIEs do not represent additional claims on the Company's general assets (Note 2).

See notes to consolidated financial statements

CHINANET ONLINE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME / (LOSS)
(In thousands)

	Three Months Ended March 31,	
	2013 (US $) (Unaudited)	2012 (US $) (Unaudited)
Sales		
From unrelated parties	$ 6,990	$ 14,920
From related parties	59	15
	7,049	14,935
Cost of sales	4,467	12,538
Gross margin	2,582	2,397
Operating expenses		
Selling expenses	788	689
General and administrative expenses	1,402	1,243
Research and development expenses	449	331
	2,639	2,263
Loss/(income) from operations	(57)	134
Other income (expenses)		
Interest income	32	5
Other expenses	(1)	(1)
	31	4
Loss/(income) before income tax expense, equity method investments and noncontrolling interests	(26)	138
Income tax benefit/(expense)	86	(236)
Income/(loss) before equity method investments and noncontrolling interests	60	(98)
Share of losses in equity investment affiliates	(71)	(193)
Net loss	(11)	(291)
Net loss/(income) attributable to noncontrolling interests	41	(75)
Net income/(loss) attributable to ChinaNet Online Holdings, Inc.	30	(366)

CHINANET ONLINE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME / LOSS CONTINUED
(In thousands, except for number of shares and per share data)

	Three Months Ended March 31, 2013 (US $) (Unaudited)	2012 (US $) (Unaudited)
Net loss	(11)	(291)
Foreign currency translation gain	215	263
Comprehensive income/(loss)	$ 204	$ (28)
Comprehensive loss/(income) attributable to noncontrolling interests	38	(112)
Comprehensive income/(loss) attributable to ChinaNet Online Holdings, Inc.	$ 242	$ (140)
Earnings/(loss) per share		
Earnings/(loss) per common share		
Basic	$ 0.00	$ (0.02)
Diluted	$ 0.00	$ (0.02)
Weighted average number of common shares outstanding:		
Basic	22,186,540	22,182,584
Diluted	22,186,540	22,182,584

See notes to consolidated financial statements

CHINANET ONLINE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Three Months Ended March 31,	
	2013 (US $) (Unaudited)	2012 (US $) (Unaudited)
Cash flows from operating activities		
Net loss	$ (11)	$ (291)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation and amortization	418	409
Share-based compensation expenses	11	17
Allowances for doubtful debts	260	-
Share of losses in equity investment affiliates	71	193
Deferred taxes	(185)	(381)
Changes in operating assets and liabilities		
Accounts receivable	(1,297)	(3,154)
Other receivables	(8)	261
Prepayment and deposit to suppliers	(406)	1,740
Due from related parties	(49)	48
Other current assets	(2)	(22)
Accounts payable	105	(56)
Advances from customers	564	1,162
Accrued payroll and other accruals	(29)	(133)
Due to related parties	-	(78)
Other payables	-	18
Taxes payable	127	630
Net cash (used in) provided by operating activities	(431)	363
Cash flows from investing activities		
Purchases of vehicles and office equipment	(11)	(9)
Project development deposit to a third party	-	(2,452)
Payment for acquisition of VIEs	(1,272)	-
Net cash used in investing activities	(1,283)	(2,461)

CHINANET ONLINE HOLDINGS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
(In thousands)

	Three Months Ended March 31,	
	2013 (US $) (Unaudited)	2012 (US $) (Unaudited)
Cash flows from financing activities		
Dividend paid to convertible preferred stockholders	-	(5)
Short-term loan borrowed from an equity investment affiliate	-	316
Net cash provided by financing activities	-	311
Effect of exchange rate fluctuation on cash and cash equivalents	23	56
Net decrease in cash and cash equivalents	(1,691)	(1,731)
Cash and cash equivalents at beginning of the period	5,483	10,695
Cash and cash equivalents at end of the period	$ 3,792	$ 8,964
Supplemental disclosure of cash flow information		
Income taxes paid	$ 4	$ 15
Non-cash transactions:		
Restricted stock and options granted for future service	$ 32	$ 74

See notes to consolidated financial statements

CHINANET ONLINE HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Organization and nature of operations

ChinaNet Online Holdings, Inc. (formerly known as Emazing Interactive, Inc.) (the "Company") was incorporated in the State of Texas in April 2006 and re-domiciled to become a Nevada corporation in October 2006. From the date of the Company's incorporation until June 26, 2009, when the Company consummated the Share Exchange (discussed below), the Company's activities were primarily concentrated in web server access and company branding in hosting web based e-games.

On June 26, 2009, the Company entered into a Share Exchange Agreement (the "Exchange Agreement"), with (i) China Net Online Media Group Limited, a company organized under the laws of British Virgin Islands ("China Net BVI"), (ii) China Net BVI's shareholders, Allglad Limited, a British Virgin Islands company ("Allglad"), Growgain Limited, a British Virgin Islands company ("Growgain"), Rise King Investments Limited, a British Virgin Islands company ("Rise King BVI"), Star (China) Holdings Limited, a British Virgin Islands company ("Star"), Surplus Elegant Investment Limited, a British Virgin Islands company ("Surplus"), Clear Jolly Holdings Limited, a British Virgin Islands company ("Clear" and together with Allglad, Growgain, Rise King BVI, Star and Surplus, the "China Net BVI Shareholders"), who together owned shares constituting 100% of the issued and outstanding ordinary shares of China Net BVI (the "China Net BVI Shares") and (iii) G. Edward Hancock, the principal stockholder of the Company at that time. Pursuant to the terms of the Exchange Agreement, the China Net BVI Shareholders transferred to the Company all of the China Net BVI Shares in exchange for the issuance of 13,790,800 shares (the "Exchange Shares") in the aggregate of the Company's common stock (the "Share Exchange"). As a result of the Share Exchange, China Net BVI became a wholly owned subsidiary of the Company and the Company is now a holding company, which, through certain contractual arrangements with operating companies in the People's Republic of China (the "PRC"), is engaged in providing advertising, marketing, communication and brand management and sales channel building services to small and medium companies in China.

The Company's wholly owned subsidiary, China Net BVI was incorporated in the British Virgin Islands on August 13, 2007. On April 11, 2008, China Net BVI became the parent holding company of a group of companies comprised of CNET Online Technology Limited, a Hong Kong company ("China Net HK"), which established and is the parent company of Rise King Century Technology Development (Beijing) Co., Ltd., a wholly foreign-owned enterprise ("WFOE") established in the PRC ("Rise King WFOE"). The Company refers to the transactions that resulted in China Net BVI becoming an indirect parent company of Rise King WFOE as the "Offshore Restructuring."

PRC regulations prohibit direct foreign ownership of business entities providing internet content, or ICP services in the PRC, and restrict foreign ownership of business entities engaging in the advertising business. In October 2008, a series of contractual arrangements (the "Contractual Agreements" or "VIE Agreements") were entered into among Rise King WFOE and Business Opportunity Online (Beijing) Network Technology Co., Ltd. ("Business Opportunity Online"), Beijing CNET Online Advertising Co., Ltd. ("Beijing CNET Online") (collectively the "PRC Operating Entities") and its common individual owners (the "PRC Shareholders" or the "Control Group"). The Contractual Agreements allowed China Net BVI, through Rise King WFOE, to, among other things, secure significant rights to influence the PRC Operating Entities' business operations, policies and management, approve all matters requiring shareholder approval, and receive 100% of the income earned by the PRC Operating Entities. In return, Rise King WFOE provides consulting services to the PRC Operating Entities. In addition, to ensure that the PRC Operating Entities and the PRC Shareholders perform their obligations under the Contractual Arrangements, the PRC Shareholders have pledged all of their equity interests in the PRC Operating Entities to Rise King WFOE. They also entered into an option agreement with Rise King WFOE which provides that at such time as when the current restrictions under PRC law on foreign ownership of Chinese companies engaging in the Internet content, information services or advertising business in China are lifted, Rise King WFOE may exercise its option to purchase the equity interests in the PRC Operating Entities, directly.

Pursuant to the Contractual Agreements, all of the equity owners' rights and obligations of the VIEs were assigned to Rise King WFOE, which resulted in the equity owners lacking the ability to make decisions that have a significant effect on the VIEs, Rise King WFOE's ability to extract the profits from the operation of the VIEs and assume the residual benefits of the VIEs. Due to the fact that Rise King WFOE and its indirect parent are the sole interest holders of the VIEs, the Company included the assets, liabilities, revenues and expenses of the VIEs in its consolidated financial statements, which is consistent with the provisions of FASB Accounting Standards Codification ("ASC") Topic 810 “Consolidation”, subtopic 10.

As of the date of the Share Exchange, through the Contractual Agreements, the Company operates its business in China primarily through Business Opportunity Online and Beijing CNET Online. Beijing CNET Online owns 51% of Shanghai Borongdingsi Computer Technology Co., Ltd. (“Shanghai Borongdingsi”). Business Opportunity Online, Beijing CNET Online and Shanghai Borongdingsi, were incorporated on December 8, 2004, January 27, 2003 and August 3, 2005, respectively.

CHINANET ONLINE HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Shanghai Borongdingsi is 51% owned by Beijing CNET Online. Beijing CNET Online and Shanghai Borongdingsi entered into a cooperation agreement in June 2008, followed up with a supplementary agreement in December 2008, to conduct a bank kiosk advertisement business. The business is based on a bank kiosk cooperation agreement between Shanghai Borongdingsi and Henan provincial branch of China Construction Bank which allows Shanghai Borongdingsi or its designated party to conduct in-door advertisement business within the business outlets throughout Henan Province. The bank kiosk cooperation agreement has a term of eight years beginning in August 2008. However, Shanghai Borongdingsi was not able to conduct the advertisement business as a stand-alone business due to the lack of an advertisement business license and supporting financial resources. Pursuant to the aforementioned cooperation agreements, Beijing CNET Online committed to purchase equipment and to provide working capital, technical and other related support to Shanghai Borongdingsi. Beijing CNET Online owns the equipment used in the kiosk business, is entitled to sign contracts in its name on behalf of the business, and holds the right to collect the advertisement revenue generated from the bank kiosk business exclusively until it recovers the cost of purchasing the equipment. Thereafter, Beijing CNET Online has agreed to distribute 49% of the net profit generated from the bank kiosk advertising business, if any, to the minority shareholders of Shanghai Borongdingsi.

On June 24, 2010, one of the Company's VIEs, Business Opportunity Online, together with three other individuals, who were not affiliated with the Company, formed a new company, Shenzhen City Mingshan Network Technology Co., Ltd. ("Shenzhen Mingshan"). Shenzhen Mingshan is 51% owned by Business Opportunity Online and 49% owned collectively by the other three individuals. Shenzhen Mingshan is primarily engaged in developing and designing internet based software, online games and the related operating websites and providing related internet and information technology services necessary to operate such games and websites. On January 6, 2011, as approved by the shareholders of Shenzhen Mingshan, an unaffiliated third party invested RMB15,000,000 (approximately US$2,387,927) into Shenzhen Mingshan in exchange for a 60% equity interest in Shenzhen Mingshan. Therefore, beginning on January 6, 2011, the new investor became the majority shareholder of Shenzhen Mingshan. The Company's share of the equity interest in Shenzhen Mingshan decreased from 51% to 20.4% and the Company ceased to have a controlling financial interest in Shenzhen Mingshan, but still retains an investment in, and significant influence over, Shenzhen Mingshan. On December 19, 2012, as approved by the shareholders of Shenzhen Mingshan, Shenzhen Mingshan reduced its registered and paid-in capital from RMB25,000,000 (approximately US$3,979,878) to RMB22,000,000 (approximately US$3,502,292), resulted from a decrease in paid-in capital from three other noncontrolling shareholders, except Business Opportunity Online. As a result, the Company's share of the equity interest in Shenzhen Mingshan increased from 20.4% to 23.18% and the Company continued to retain significant influence over Shenzhen Mingshan.

On December 6, 2010, Rise King WFOE entered into a series of exclusive contractual arrangements, which were similar to the Contractual Agreements discussed above, with Rise King (Shanghai) Advertisement Media Co., Ltd. ("Shanghai Jing Yang"), a company incorporated under the PRC laws in December 2009 and primarily engaged in the advertising business, pursuant to which the Company, through its wholly owned subsidiary, Rise King WFOE obtained all of the equity owners' rights and obligations of Shanghai Jing Yang, and the ability to extract the profits from the operation and assume the residual benefits of Shanghai Jing Yang, and hence became the sole interest holder of Shanghai Jing Yang. As of the date these contractual agreements were entered into, Shanghai Jing Yang did not have the resources necessary to conduct any business activities by itself and the carrying amount of the net assets of Shanghai Jing Yang which was all cash and cash equivalents approximate its fair value due to their short maturities. Therefore, Shanghai Jing Yang's accounts were included in the Company's consolidated financial statements with no goodwill recognized in accordance with ASC Topic 810 "Consolidation".

The Company, through one of its VIEs, Beijing CNET Online, acquired a 100% equity interest in Quanzhou Zhi Yuan Marketing Planning Co., Ltd. ("Quanzhou Zhi Yuan") and a 51% equity interest in Quanzhou Tian Xi Shun He

Advertisement Co., Ltd. ("Quanzhou Tian Xi Shun He") on January 4, 2011 and February 23, 2011, respectively. Quanzhou Zhi Yuan and Quanzhou Tian Xi Shun He are both independent advertising companies based in Fujian province of the PRC, which provide comprehensive branding and marketing services to over fifty small to medium sized companies focused primarily in the sportswear and clothing industry. In June 2011, Beijing CNET Online acquired the remaining 49% equity interest in Quanzhou Tian Xi Shun He. Quanzhou Tian Xi Shun He became a wholly owned subsidiary of Beijing CNET Online accordingly.

CHINANET ONLINE HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

On January 28, 2011, one of the Company's VIEs, Business Opportunity Online, formed a new wholly owned subsidiary, Business Opportunity Online (Hubei) Network Technology Co., Ltd. ("Business Opportunity Online Hubei"). Business Opportunity Online Hubei is primarily engaged in internet advertisement design, production and promulgation.

On March 1, 2011, one of the Company's VIEs, Business Opportunity Online, together with an individual, who was not affiliated with the Company, formed a new company, Beijing Chuang Fu Tian Xia Network Technology Co., Ltd. ("Beijing Chuang Fu Tian Xia"). Beijing Chuang Fu Tian Xia is 51% owned by Business Opportunity Online and 49% owned by the co-founding individual. In addition to capital investment, the co-founding individual is required to provide the controlled domain names, www.liansuo.com and www.chuangye.com to be registered under the established company. Beijing Chuang Fu Tian Xia is primarily engaged in providing and operating internet advertising, marketing and communication services to small and medium companies through the websites associated the above mentioned domain names.

On April 18, 2011, the Company, through one of its VIEs, Business Opportunity Online Hubei formed a new wholly owned company, Hubei CNET Advertising Media Co., Ltd. ("Hubei CNET"). Hubei CNET is primarily engaged in advertisement design, production, promulgation and providing the related advertising and marketing consultancy services.

On April 18, 2011, one of the Company's VIEs, Business Opportunity Online Hubei, together with an individual, who was not affiliated with the Company, formed a new company, Zhao Shang Ke Network Technology (Hubei) Co., Ltd. ("Zhao Shang Ke Hubei"). Zhao Shang Ke Hubei is 51% owned by Business Opportunity Online Hubei and 49% owned by the co-founding individual. Zhao Shang Ke Hubei is primarily engaged in providing advertisement design, production, promulgation and brand management and sales channels building services. On December 29, 2011, as approved by the shareholders of Zhao Shang Ke Hubei, two unaffiliated third party investors invested RMB10,000,000 (approximately US$1,591,951) into Zhao Shang Ke Hubei in exchange for an aggregate 50% equity interest in Zhao Shang Ke Hubei. Therefore, beginning on December 29, 2011, the Company's share of the equity interest in Zhao Shang Ke Hubei decreased from 51% to 25.5%. As such, the Company ceased to have a controlling financial interest in Zhao Shang Ke Hubei, but still retained an investment in, and significant influence over, Zhao Shang Ke Hubei.

On July 1, 2011, one of the Company's VIEs, Quanzhou Zhi Yuan, formed a new wholly owned company, Xin Qi Yuan Advertisement Planning (Hubei) Co., Ltd. ("Xin Qi Yuan Hubei"). Xin Qi Yuan Hubei is primarily engaged in advertisement design, production, promulgation and providing the related advertising and marketing consultancy services.

On July 1, 2011, one of the Company's VIEs, Quanzhou Tian Xi Shun He, formed a new wholly owned company, Mu Lin Sen Advertisement (Hubei) Co., Ltd. ("Mu Lin Sen Hubei"). Mu Lin Sen Hubei is primarily engaged in advertisement design, production, promulgation and providing the related advertising and marketing consultancy services.

On July 1, 2011, one of the Company's VIEs, Business Opportunity Online Hubei, together with an individual who is not affiliated with the Company, formed a new company, Sheng Tian Network Technology (Hubei) Co., Ltd. ("Sheng Tian Hubei"). Sheng Tian Hubei is 51% owned by Business Opportunity Online Hubei and 49% owned by the co-founding individual. Sheng Tian Hubei is primarily engaged in computer system design, development and promotion, software development and promotion, and providing the related technical consultancy services.

On December 20, 2011, one of the Company's VIEs, Business Opportunity Online Hubei acquired a 51% equity interest in Sou Yi Lian Mei Network Technology (Beijing) Co. Ltd., ("Sou Yi Lian Mei"). In September 2012, Business Opportunity Online Hubei acquired the remaining 49% equity interest in Sou Yi Lian Mei. Sou Yi Lian Mei became a wholly owned subsidiary of Business Opportunity Online Hubei accordingly. Sou Yi Lian Mei is primary engaged in providing online advertising and marketing services and operates its business primarily through its wholly-owned subsidiary, Jin Du Ya He (Beijing) Network Technology Co., Ltd ("Jin Du Ya He").

As of March 31, 2013, the Company operated its business primarily in China through its PRC subsidiary and PRC operating entities, or VIEs as described above.

CHINANET ONLINE HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

2. Variable Interest Entities

To satisfy PRC laws and regulations, the Company conducts certain business in the PRC through its Variable Interest Entities ("VIEs"). Summarized below is the information related to the consolidated VIEs' assets and liabilities as of March 31, 2013 and December 31, 2012, respectively:

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Assets		
Current assets:		
Cash and cash equivalents	$ 2,642	$ 4,275
Term deposit	3,375	3,357
Accounts receivable, net	9,778	8,392
Other receivables, net	2,988	2,921
Prepayment and deposit to suppliers	14,820	14,587
Due from related parties	57	49
Other current assets	37	35
Deferred tax assets-current	42	50
Total current assets	33,739	33,666
Investment in and advance to equity investment affiliates	849	916
Property and equipment, net	1,284	1,389
Intangible assets, net	6,934	7,152
Goodwill	11,144	11,083
Deferred tax assets-non current	613	511
Total Assets	$ 54,563	$ 54,717
Liabilities		
Current liabilities:		
Accounts payable	$ 219	$ 110
Advances from customers	1,635	1,065
Accrued payroll and other accruals	375	455
Due to Control Group	11	11
Payable for acquisition	-	1,266
Taxes payable	6,316	6,136
Other payables	199	196
Total current liabilities	8,755	9,239
Deferred tax Liabilities-non current	1,643	1,689
Total Liabilities	$ 10,398	$ 10,928

All of the VIEs' assets can be used to settle obligations of their primary beneficiary. Liabilities recognized as a result of consolidating these VIEs do not represent additional claims on the Company's general assets.

For the three months ended March 31, 2013, the financial performance of the VIEs reported in the Company's consolidated statements of income and comprehensive income includes sales of approximately US$6,950,000, cost of sales of approximately US$4,467,000, operating expenses of approximately US$2,090,000 and net income before allocation to noncontrolling interests of approximately US$400,000.

For the three months ended March 31, 2012, the financial performance of the VIEs reported in the Company's consolidated statements of income and comprehensive loss includes sales of approximately US$14,896,000, cost of sales of approximately US$12,536,000, operating expenses of approximately US$1,655,000 and net income before allocation to noncontrolling interests of approximately US$233,000.

CHINANET ONLINE HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. Summary of significant accounting policies

a) Basis of presentation

The interim consolidated financial statements are prepared and presented in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

The interim consolidated financial information as of March 31, 2013 and for the three months ended March 31, 2013 and 2012 have been prepared without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Certain information and footnote disclosures, which are normally included in annual consolidated financial statements prepared in accordance with U.S. GAAP, have been omitted pursuant to those rules and regulations. The interim consolidated financial information should be read in conjunction with the financial statements and the notes thereto, included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, previously filed with the SEC.

In the opinion of management, all adjustments (which include normal recurring adjustments) necessary to present a fair statement of the Company's consolidated financial position as of March 31, 2013, its consolidated results of operations for the three months ended March 31, 2013 and 2012, and its consolidated cash flows for the three months ended March 31, 2013 and 2012, as applicable, have been made. The interim results of operations are not necessarily indicative of the operating results for the full fiscal year or any future periods.

b) Principles of consolidation

The interim consolidated financial statements include the financial statements of all the subsidiaries and VIEs of the Company. All transactions and balances between the Company and its subsidiaries and VIEs have been eliminated upon consolidation. According to the agreements between Beijing CNET Online and Shanghai Borongdingsi, although Beijing CNET Online legally owns 51% of Shanghai Borongdingsi's interests, Beijing CNET Online only controls the assets and liabilities related to the bank kiosks business, which has been included in the financial statements of Beijing CNET Online, but does not control other assets of Shanghai Borongdingsi, thus, Shanghai Borongdingsi's financial statements were not consolidated by the Company.

c) Use of estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the related disclosure of contingent assets and liabilities at the date of these consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. The Company continually evaluates these estimates and assumptions based on the most recently available information, historical experience and various other assumptions that the Company believes to be reasonable under the circumstances. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates.

d) Foreign currency translation and transactions

The functional currency of the Company is United States dollars ("US$"), and the functional currency of China Net HK is Hong Kong dollars ("HK$"). The functional currency of the Company's PRC operating subsidiary and VIEs is Renminbi ("RMB"), and PRC is the primary economic environment in which the Company operates.

For financial reporting purposes, the financial statements of the Company's PRC operating subsidiary and VIEs, which are prepared using the RMB, are translated into the Company's reporting currency, the United States Dollar ("U.S. dollar"). Assets and liabilities are translated using the exchange rate at each balance sheet date. Revenue and expenses are translated using average rates prevailing during each reporting period, and stockholders' equity is translated at historical exchange rates. Adjustments resulting from the translation are recorded as a separate component of accumulated other comprehensive income in stockholders' equity.

Transactions denominated in currencies other than the functional currency are translated into the functional currency at the exchange rates prevailing at the dates of the transactions. The resulting exchange differences are included in the determination of net income of the consolidated statements of income and comprehensive income for the respective periods.

CHINANET ONLINE HOLDINGS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

The exchange rates used to translate amounts in RMB into US$ for the purposes of preparing the consolidated financial statements are as follows:

	March 31, 2013	December 31, 2012
Balance sheet items, except for equity accounts	6.2816	6.3161

	Three Months Ended March 31, 2013	2012
Items in the statements of income and comprehensive income, and statements of cash flows	6.2858	6.3201

No representation is made that the RMB amounts could have been, or could be converted into US$ at the above rates.

e) Advertising costs

Advertising costs for the Company's own brand building are not includable in cost of sales, they are expensed when incurred or amortized over the estimated beneficial period and are included in "selling expenses" in the statement of income and comprehensive income. For the three months ended March 31, 2013 and 2012, advertising expenses for the Company's own brand building were approximately US$24,000 and US$74,000, respectively.

f) Research and development expenses

The Company accounts for the cost of developing and upgrading technologies and platforms and intellectual property that are used in its daily operations in research and development cost. Research and development costs are charged to expense when incurred. Expenses for research and development for the three months ended March 31, 2013 and 2012 were approximately US$449,000 and US$ 331,000, respectively.

g) Income taxes

The Company follows the guidance of ASC Topic 740 "Income taxes" and uses liability method to account for income taxes. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial reporting and tax bases of assets and liabilities using enacted tax rates that will be in effect in the period in which the differences are expected to reverse. The Company records a valuation allowance to offset deferred tax assets, if based on the weight of available evidence, it is more-likely-than-not that some portion, or all, of the deferred tax assets will not be realized. The effect on deferred taxes of a change in tax rates is recognized in statement of income and comprehensive income in the period that includes the enactment date.

h) Uncertain tax positions

The Company follows the guidance of ASC Topic 740 "Income taxes", which prescribes a more likely than not threshold for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on recognition of income tax assets and liabilities, classification of current and deferred income tax assets and liabilities, accounting for interest and penalties associated with tax positions, accounting for income taxes in interim periods, and income tax disclosures.

The Company recognizes interest on non-payment of income taxes under requirement by tax law and penalties associated with tax positions when a tax position does not meet the minimum statutory threshold to avoid payment of penalties. According to the PRC Tax Administration and Collection Law, the statute of limitations is three years if the underpayment of taxes is due to computational errors made by the taxpayer or the withholding agent. The statute of limitations is extended to five years under special circumstances, where the underpayment of taxes is more than RMB100,000. In the case of transfer pricing issues, the statute of limitation is ten years. There is no statute of limitation in the case of tax evasion. The tax returns of the Company's PRC subsidiary and VIEs are subject to examination by the relevant tax authorities. The Company did not have any material interest or penalties associated with tax positions for the three months ended March 31, 2013 and 2012, and did not have any significant unrecognized uncertain tax positions as of March 31, 2013 and December 31, 2012, respectively.

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i) Recent accounting standards

In February 2013, the FASB issued Accounting Standards Update ("ASU") 2013-02, "Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income". The ASU does not change the current requirements for reporting net income or other comprehensive income in financial statements. However, this ASU requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. The guidance is effective prospectively for reporting periods beginning after December 15, 2012 for public entities. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position or results of operations.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on the Company's consolidated financial statements upon adoption.

4. Cash and cash equivalent

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Cash	801	893
Bank deposit	2,991	4,590
	3,792	5,483

5. Term deposit

Term deposit as of March 31, 2013 represented the amount of cash placed as a term deposit by one of the Company's operating VIEs in a major financial institution of China, which management believes is of high credit quality. The interest rate of the term deposit is 3.5% per annual and the term deposit will mature on July 5, 2013.

6. Accounts receivable, net

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Accounts receivable	13,481	12,116

Allowance for doubtful debts	(3,650)	(3,630)
Accounts receivable, net	9,831	8,486

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All of the accounts receivable are non-interest bearing. Based on the assessment of the collectability of the accounts receivable as of March 31, 2013, the Company provided approximately US$3,650,000 allowance for doubtful debts, which were related to the accounts receivable of the Company’s internet advertising and TV advertising business segment with an aging over six months. For the three months ended March 31, 2013, no additional allowance for doubtful debts was provided.

7. Other receivables, net

	March 31, 2013 US$(’000) (Unaudited)	December 31, 2012 US$(’000)
Short-term loan made for marketing campaign	2,388	2,375
Short-term loans to unrelated entities	478	475
Term deposit interest receivable	89	59
Staff advances for normal business purpose	173	194
Overdue contract guarantee deposits	420	158
Allowance for doubtful debts	(420)	(158)
Other receivables, net	3,128	3,103

Short-term loan for marketing campaign: for one of the major marketing campaigns, the Company made a marketing-related loan of RMB25,000,000 (approximately US$3,979,878) to a TV series of 36 episodes, called “Xiao Zhang Feng Yun.” This TV series was produced in commemoration of “The Republican Revolution of 1911” (the Chinese bourgeois democratic revolution led by Dr. Sun Yat-sen which overthrew the Qing Dynasty). By participating in this TV series, the Company’s logo will be shown during the credits at the end of each episode and also shown as a separate card during the closing before the credit screen. This TV series has been broadcasted on CCTV 8 and www.sina.com.cn since September 2011 and continues to sell its broadcasting rights to other provincial TV channels for additional exposure. For the years ended December 31, 2012 and 2011, the Company has collected an aggregate of RMB10,000,000 (approximately US$1,591,951) from the borrower. In accordance with the communication between the Company and the borrower, the Company has extended the term of this loan from December 31, 2012 to December 31, 2013, as this TV series is still selling its broadcasting rights to TV stations and other media and the Company has agreed a repayment schedule with the borrower, which is within one year. The Company will continue to assess the collectability of this loan and if an event occurs or circumstances change that could indicate that the collectability of this loan is remote, a full allowance of bad debts provision will be provided for the remaining outstanding balance of this loan.

For all advertising resources purchasing contracts signed by the Company with its resource providers, the Company is required to make contract guarantee deposits, which are either used to pay the actual contract amount of resources used in the last month of each contract period or to be refunded to the Company of the remaining balance upon expiration of the contract. Overdue contract guarantee deposits represented the portion of the contract guarantee deposits, which related advertising resources purchasing contracts had been completed as of each of the reporting dates. Based on the assessment of the collectability of these overdue contract guarantee deposits as of March 31, 2013, the Company provided approximately US$420,000 allowance for doubtful debts, which was related to the contract guarantee deposits of its TV advertising business segment. For the three months ended March 31, 2013, approximately

US$260,000 allowance for doubtful debts was provided.

8. Prepayments and deposit to suppliers

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Contract execution guarantees to TV advertisement and internet resources providers	8,367	9,463
Prepayments to TV advertisement and internet resources providers	6,372	5,069
Other deposits and prepayments	83	64
	14,822	14,596

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Contract execution guarantees to TV advertisement and internet resource providers are paid as contractual deposits to the Company's resources and services providers. These amounts will be used to offset the contact amount and service fee needed to be paid for the resources and services provided in the last month of each contract period or refunded to the Company upon expiration of the purchase contracts.

According to the contracts signed between the Company and its suppliers, the Company is normally required to pay the contract amount in advance. These prepayments will be transferred to cost of sales when the related services are provided.

9. Due from related parties

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Beijing Fengshangyinli Technology Co., Ltd.	46	53
Beijing Saimeiwei Food Equipment Technology Co., Ltd.	134	87
Beijing Telijie Century Environmental Technology Co., Ltd.	80	70
	260	210

These related parties are directly or indirectly owned by Mr. Handong Cheng, Mr. Xuanfu Liu or Ms. Li Sun (acting as nominee for Mr. Zhige Zhang), the owners of the Company's PRC VIEs, Business Opportunities Online and Beijing CNET Online before the Offshore Restructuring. The Company provides advertising services to these related parties in its normal course of business on the same terms as those provided to its unrelated advertising clients. Due from related parties represented the outstanding receivables for the advertising services that the Company provided to these related parties as of each of the reporting date.

10. Investment in and advance to equity investment affiliates

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Investment in equity investment affiliates	849	916
Advance to equity investment affiliates	43	43
	892	959

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The following table summarizes the movement of the investment in and advance to equity investment affiliates for the three months ended March 31, 2013:

	Shenzhen Mingshan US$('000)	Zhao Shang Ke Hubei US$('000)	Total US$('000)
Balance as of December 31, 2012 (audited)	492	467	959
Share of losses in equity investment affiliates	(26)	(45)	(71)
Exchange translation adjustment	2	2	4
Balance as of March 31, 2013 (unaudited)	468	424	892

Shenzhen Mingshan:

Shenzhen Mingshan was incorporated on June 24, 2010 by one of the Company's VIEs, Business Opportunities Online and three other individuals who were not affiliated with the Company. Shenzhen Mingshan was 51% owned by the Company and was a consolidated VIE of the Company from the date of incorporation through January 6, 2011. On January 6, 2011, an unaffiliated third party invested RMB15,000,000 (approximately US$2,387,927) into Shenzhen Mingshan in exchange for a 60% equity interest in Shenzhen Mingshan. The Company's share of equity interest decreased from 51% to 20.4% accordingly. On December 19, 2012, as approved by the shareholders of Shenzhen Mingshan, Shenzhen Mingshan reduced its registered and paid-in capital from RMB25,000,000 (approximately US$3,979,878) to RMB22,000,000 (approximately US$3,502,292), resulted from a decrease of paid-in capital from three other noncontrolling shareholders, except Business Opportunity Online. As a result, the Company's share of the equity interest in Shenzhen Mingshan increased from 20.4% to 23.18% and the Company continued to retain significant influence over Shenzhen Mingshan.

For the three months ended March 31, 2013 and 2012, the Company recognized its pro-rata shares of losses in Shenzhen Mingshan of approximately US$26,000 and US$83,000, respectively. These losses recognized were reflected in the caption of "Share of losses in equity investment affiliates" in the Company's consolidated statements of income and comprehensive income with a corresponding decrease to the carrying value of the investment in Shenzhen Mingshan in the Company's consolidated balance sheets.

Zhao Shang Ke Hubei:

Zhao Shang Ke Hubei was incorporated on April 18, 2011 by one of the Company's VIEs, Business Opportunities Online Hubei and a co-founding individual who was not affiliated with the Company. Zhao Shang Ke Hubei was 51% owned by the Company and was a consolidated subsidiary of the Company from the date of incorporation through December 29, 2011. On December 29, 2011, two unaffiliated third party investors invested RMB10,000,000 (approximately US$1,591,951) in cash into Zhao Shang Ke Hubei in exchange for an aggregate 50% equity interest in Zhao Shang Ke Hubei. The Company's share of equity interest decreased from 51% to 25.5% accordingly.

For the three months ended March 31, 2013 and 2012, the Company recognized its pro-rata share of losses in Zhao Shang Ke Hubei of approximately US$45,000 and US$110,000, respectively, which was reflected in the caption of "Share of losses in equity investment affiliates" in the Company's consolidated statements of income and comprehensive income with a corresponding decrease to the carrying value of the investment in Zhao Shang Ke Hubei in the Company's consolidated balance sheets.

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11. Property and equipment, net

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Vehicles	930	925
Office equipment	1,500	1,481
Electronic devices	1,212	1,205
Property and equipment, cost	3,642	3,611
Less: accumulated depreciation	(2,141)	(1,975)
Property and equipment, net	1,501	1,636

Depreciation expenses in the aggregate for the three months ended March 31, 2013 and 2012 were approximately US$155,000 and $148,000, respectively.

12. Intangible assets, net

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Intangible assets not subject to amortization:		
Trade name	311	309
Domain name	1,538	1,529
Intangible assets subject to amortization:		
Contract backlog	197	196
Customer relationship	3,453	3,434
Non-compete agreements	1,366	1,358
Software technologies	326	325
Cloud-computing based software platforms	1,478	1,470
Other computer software	76	76
Intangible assets, cost	8,745	8,697
Less: accumulated amortization	(1,801)	(1,530)
Intangible assets, net	6,944	7,167

Amortization expenses in aggregate for the three months ended March 31, 2013 and 2012 were approximately US$263,000 and US$262,000, respectively.

Based on the carrying value of the finite-lived intangible assets recorded as of March 31, 2013, and assuming no subsequent impairment of the underlying intangible assets, the estimated future amortization expenses is approximately US$771,000 for the nine months ended December 31, 2013, approximately US$1,027,000 per year through December 31, 2015, approximately US$988,000 for the year ended December 31, 2016 and approximately US$498,000 for the year ended December 31, 2017.

13. Goodwill

	Amount US$('000)
Balance as of December 31, 2012 (audited)	11,083
Exchange translation adjustment	61
Balance as of March 31, 2013 (unaudited)	11,144

CHINANET ONLINE HOLDINGS, INC.
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14. Accrued payroll and other accruals

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Accrued payroll and staff welfare	460	538
Accrued operating expenses	417	366
	877	904

15. Payable for acquisition

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Sou Yi Lian Mei	-	1,266

Payable for acquisition as of December 31, 2012 represented the outstanding balance payment of approximately RMB8.0 million for the acquisition of the 49% equity interest of Sou Yi Lian Mei that was consummated in September 2012, which was paid to the former shareholder of Sou Yi Lian Mei during the three months ended March 31, 2013.

16. Taxation

1) Income tax

The entities within the Company file separate tax returns in the respective tax jurisdictions in which they operate.

i). The Company is incorporated in the state of Nevada. Under the current law of Nevada, the Company is not subject to state corporate income tax. Following the Share Exchange, the Company became a holding company and does not conduct any substantial operations of its own. No provision for federal corporate income tax has been made in the financial statements as the Company has no assessable profits for the three months ended March 31, 2013, or any prior periods. The Company does not provide for U.S. taxes or foreign withholding taxes on undistributed earnings from its non-U.S. subsidiaries because such earnings are intended to be reinvested indefinitely. If undistributed earnings were distributed, foreign tax credits could become available under current law to reduce the resulting U.S. income tax liability.

ii). China Net BVI was incorporated in the British Virgin Islands ("BVI"). Under the current law of the BVI, China Net BVI is not subject to tax on income or capital gains. Additionally, upon payments of dividends by China Net BVI to its shareholders, no BVI withholding tax will be imposed.

iii). China Net HK was incorporated in Hong Kong and does not conduct any substantial operations of its own. No provision for Hong Kong profits tax has been made in the financial statements as China Net HK has no assessable profits for the three months ended March 31, 2013 or any prior periods. Additionally, upon payments of dividends by China Net HK to its shareholders, no Hong Kong withholding tax will be imposed.

iv). The Company's PRC operating subsidiary and VIEs, being incorporated in the PRC, are governed by the income tax law of the PRC and is subject to PRC enterprise income tax ("EIT"). The EIT rate of PRC is 25%, which applies to both domestic and foreign invested enterprises.

- Rise King WFOE is a software company qualified by the related PRC governmental authorities and was approved by the local tax authorities of Beijing, the PRC, to be entitled to a two-year EIT exemption from its first profitable year and a 50% reduction of its applicable EIT rate, which is 25% to 12.5% of its taxable income for the succeeding three years. Rise King WFOE had a net loss for the year ended December 31, 2008 and its first profitable year was fiscal year 2009 which has been verified by the local tax bureau by accepting the application filed by the Company. Therefore, it was approved to be entitled to a two-year EIT exemption for fiscal year 2009 through fiscal year 2010 and a 50% reduction of its applicable EIT rate which is 25% to 12.5% for fiscal year 2011 through fiscal year 2013. Therefore, for the three months ended March 31, 2013 and 2012, the applicable income tax rate for Rise King WFOE was both 12.5%. After fiscal year 2013, the applicable income tax rate for Rise King WFOE will be 25% under the current EIT law of PRC.

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- Business Opportunity Online was approved by the related PRC governmental authorities as a High and New Technology Enterprise under the current EIT law, and was approved by the local tax authorities of Beijing, the PRC, to be entitled to a favorable statutory tax rate of 15%. Business Opportunity Online's High and New Technology Enterprise certificate would expire on September 4, 2012. On July 9, 2012, Business Opportunity Online passed the administrative review conducted by the related PRC governmental authorities for obtaining the renewed certificate, which enabled it to continue to enjoy the 15% preferential income tax rate as a High and New Technology Enterprise. Therefore, for the three months ended March 31, 2013 and 2012, the applicable income tax rate of Business Opportunity Online was both 15%.

- Business Opportunity Online Hubei was incorporated in Xiaotian Industrial Park of Xiaogan Economic Development Zone in Xiaogan City, Hubei province of the PRC in 2011. On June 15, 2012, Business Opportunity Online Hubei was approved by the related PRC governmental authorities to be qualified as a software company and was approved by the local tax authorities of Xiaogan City, Hubei province, the PRC, to be entitled to a two-year EIT exemption for fiscal year 2012 and 2013, and a 50% reduction of its applicable EIT rate which is 25% to 12.5% of its taxable income for the succeeding three years until December 31, 2016. Therefore, for the three months ended March 31, 2013, the applicable income tax rate of Business Opportunity Online Hubei is nil%. For the three months ended March 31, 2012, Business Opportunity Online Hubei was still in the process of applying its software company qualification. Therefore, Business Opportunity Online Hubei accrued its income tax expense for the period using a 25% income tax rate, which was subsequently reversed upon being qualified as a software company in June 2012.

- The applicable income tax rate for other PRC operating entities of the Company is 25% for the three months ended March 31, 2013 and 2012.

- The current EIT law also imposed a 10% withholding income tax for dividends distributed by a foreign invested enterprise to its immediate holding company outside China. A lower withholding tax rate will be applied if there is a tax treaty arrangement between mainland China and the jurisdiction of the foreign holding company. Holding companies in Hong Kong, for example, will be subject to a 5% rate. Rise King WFOE is invested by immediate holding company in Hong Kong and will be entitled to the 5% preferential withholding tax rate upon distribution of the dividends to its immediate holding company.

For the three months ended March 31, 2013 and 2012, all of the preferential income tax treatments enjoyed by the Company's PRC subsidiary and VIEs were based on the current applicable laws and regulations of the PRC and approved by the related government regulatory authorities and local tax authorities where the Company's respective PRC subsidiary and VIEs operate in. Rise King WFOE, Business Opportunity Online and Business Opportunity Online Hubei were most affected by these preferential income tax treatments within the structure of the Company. The preferential income tax treatments are subject to change in accordance with the PRC government economic development policies and regulations. These preferential income tax treatments are primarily determined by the regulation and policies of the PRC government in the context of the overall economic policy and strategy. As a result, the uncertainty of theses preferential income tax treatments are subject to, but not limited to, the PRC government policy on supporting any specific industry's development under the outlook and strategy of overall macroeconomic development.

2) Turnover taxes and the relevant surcharges

From January 1, 2012 through August 31, 2012 (for the Company's PRC operating entities incorporated in Beijing) or October 31, 2012 (for the Company's PRC operating entities incorporated in Fujian province) or November 30, 2012 (for the Company's PRC operating entities incorporated in Hubei province), revenue from advertising services is subject to 5.6%-5.7% business tax (including surcharges), depending on which tax jurisdiction the Company's PRC operating subsidiary and VIE operate in, and 3% cultural industry development surcharge of the net service income after deducting amount paid to ending media promulgators. Revenue from internet technical services was subjected to 5.6%-5.7% business tax (including surcharges), depending on which tax jurisdiction the Company's PRC operating subsidiary and VIE operate in.

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On July 31, 2012, the Ministry of Finance (the “MOF”) and the State Administration of Taxation (the “SAT”) of the PRC jointly promulgated a “Circular on Launching the Pilot Collection of Value Added Tax in lieu of Business Tax in Transportation and Certain Areas of Modern Services Industries in Eight Provinces and Municipalities Including Beijing” (“Circular Cai Shui [2012] No. 71”), pursuant to which a business tax to value added tax (the “VAT”) transformation pilot program was launched. The implementation date for Beijing is September 1, 2012, for Fujian province, November 1, 2012, and for Hubei province, December 1, 2012. Other circulars such as “Circular on Carrying out the Pilot Collection of Value Added Tax in Lieu of Business Tax to be imposed on Transportation Industry and Part of Modern Services Industry in Shanghai” (“Circular Cai Shui [2011] No. 111”) jointly promulgated by the MOF and the SAT on November 16, 2011 which contains detailed implementation measures for such VAT pilot program apply to the locations including Beijing, Fujian province and Hubei province. In accordance with the Circular Cai Shui [2011] No. 111, the VAT rate for provision of modern services (other than lease of corporeal movables) is 6% and for small scale taxpayer, 3%. Therefore, beginning on September 1, 2012, for the Company’s PRC operating subsidiary and VIEs incorporated in Beijing, November 1, 2012, for the Company’s PRC operating VIEs incorporated in Fujian province, and December 1, 2012, for the Company’s PRC operating VIEs incorporated in Hubei province, service revenues are subject to VAT at a rate of 6%, after deducting the VAT paid for the services purchased from suppliers, or at a rate of 3% without any deduction of VAT paid for the services purchased from suppliers. The surcharges of the VAT is 12%-14% of the VAT, depending on which tax jurisdiction the Company’s PRC operating subsidiary and VIE operate in.

Business tax is a price including tax in the PRC turnover tax system, which is calculated based on the revenue inclusive of turnover tax. Therefore, revenues achieved by the Company which are subject to business tax are presented on a gross basis inclusive of business tax, and on the other hand, business tax was included in cost of revenues upon recognition of services revenues. Contrastively, VAT is a price excluding tax in the PRC turnover tax system, which is calculated based on the revenue exclusive of turnover tax. Therefore, revenues achieved by the Company which are subject to VAT is presented on a net basis exclusive of VAT.

As of March 31, 2013 and December 31, 2012, taxes payable consists of:

	March 31, 2013 US$(’000) (Unaudited)	December 31, 2012 US$(’000)
Turnover tax and surcharge payable	2,656	2,609
Enterprise income tax payable	4,190	4,074
	6,846	6,683

For the three months ended March 31, 2013 and 2012, the Company’s income tax benefit / (expense) consisted of:

	Three Months Ended March 31,	
	2013 US$(’000) (Unaudited)	2012 US$(’000) (Unaudited)
Current-PRC	(99)	(617)

Deferred-PRC	185	381
	86	(236)

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The Company's deferred tax liabilities at March 31, 2013 and changes for the three months then ended were as follows:

	Amount US$('000)
Balance as of December 31, 2012 (audited)	1,689
Reversal during the period	(55)
Exchange translation adjustment	9
Balance as of March 31, 2013 (unaudited)	1,643

Deferred tax liabilities arose on the recognition of the identifiable intangible assets acquired from acquisition transactions and deconsolidation of subsidiaries consummated in 2011. Reversal for the three months ended March 31, 2013 of approximately US$55,000 was due to amortization of the acquired intangible assets.

The Company's deferred tax assets at March 31, 2013 and December 31, 2012 were as follows:

	March 31, 2013 US$('000) (Unaudited)	December 31, 2012 US$('000)
Tax effect of net operating losses carried forward	3,110	2,929
Bad debts provision	895	824
Valuation allowance	(3,169)	(3,051)
	836	702

March 31,
2013