

ASIAINFO-LINKAGE, INC  
Form 10-Q  
August 09, 2013  
Table of Contents

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

**FORM 10-Q**

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

For the quarterly period ended June 30, 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 001-15713

**ASIAINFO-LINKAGE, INC.**

(Exact name of registrant as specified in its charter)

Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

**DELAWARE**  
(State or other jurisdiction of  
incorporation or organization)

**752506390**  
(I.R.S. Employer  
Identification No.)

**4TH FLOOR, ZHONGDIAN INFORMATION TOWER**

**6 ZHONGGUANCUN SOUTH STREET, HAIDIAN DISTRICT**

**BEIJING 100086, CHINA**

(Address of principal executive offices, including zip code)

**+8610 8216 6688**

(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 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 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 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 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

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

The number of shares of the registrant's common stock outstanding as of July 31, 2013 was 72,876,568.

**Table of Contents**

ASIAINFO-LINKAGE, INC.

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2013

TABLE OF CONTENTS

	Page
<b><u>PART I. FINANCIAL INFORMATION</u></b>	<b>1</b>
Item 1. <b><u>Financial Statements (unaudited)</u></b>	<b>1</b>
a) <b><u>Condensed Consolidated Statements of Operations for the three months and six months ended June 30, 2013 and 2012</u></b>	<b>1</b>
b) <b><u>Condensed Consolidated Statements of Comprehensive Income for the three months and six months ended June 30, 2013 and 2012</u></b>	<b>2</b>
c) <b><u>Condensed Consolidated Balance Sheets as of June 30, 2013 and December 31, 2012</u></b>	<b>3</b>
d) <b><u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2013 and 2012</u></b>	<b>4</b>
e) <b><u>Condensed Consolidated Statements of Changes in Equity for the six months ended June 30, 2013 and the year ended December 31, 2012</u></b>	<b>5</b>
f) <b><u>Notes to Condensed Consolidated Financial Statements</u></b>	<b>6</b>
Item 2. <b><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b>	<b>28</b>
Item 3. <b><u>Quantitative and Qualitative Disclosures About Market Risk</u></b>	<b>45</b>
Item 4. <b><u>Controls and Procedures</u></b>	<b>45</b>
<b><u>PART II. OTHER INFORMATION</u></b>	<b>46</b>
Item 1. <b><u>Legal Proceedings</u></b>	<b>46</b>
Item 6. <b><u>Exhibits</u></b>	<b>46</b>
<b><u>SIGNATURE</u></b>	<b>47</b>
<b><u>EXHIBIT INDEX</u></b>	<b>48</b>

**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****ASIAINFO-LINKAGE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)**

(U.S. dollars in thousands, except share and per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
<b>Revenues:</b>				
Software products and solutions	\$ 127,554	\$ 116,772	\$ 257,027	\$ 230,834
Service	8,909	7,553	14,775	14,507
Third-party hardware	3,745	1,946	11,431	4,627
<b>Total revenues</b>	<b>140,208</b>	<b>126,271</b>	<b>283,233</b>	<b>249,968</b>
<b>Cost of revenues:</b>				
Software products and solutions	79,469	71,801	160,644	140,340
Service	4,764	3,985	9,676	8,162
Third-party hardware	3,557	1,848	10,859	4,395
<b>Total cost of revenues</b>	<b>87,790</b>	<b>77,634</b>	<b>181,179</b>	<b>152,897</b>
<b>Gross profit</b>	<b>52,418</b>	<b>48,637</b>	<b>102,054</b>	<b>97,071</b>
<b>Operating expenses (income):</b>				
Sales and marketing	20,301	18,440	38,912	38,788
General and administrative	6,685	7,826	14,933	15,304
Research and development	22,264	20,394	42,098	38,491
Government subsidies	(273)	0	(273)	0
Impairment of goodwill	286,782	0	286,782	0
<b>Total operating expenses</b>	<b>335,759</b>	<b>46,660</b>	<b>382,452</b>	<b>92,583</b>
<b>(Loss) income from operations</b>	<b>(283,341)</b>	<b>1,977</b>	<b>(280,398)</b>	<b>4,488</b>
<b>Other income (expenses), net</b>				
Interest income	1,836	2,032	3,992	4,429
Dividend income	103	604	201	604
Gain from sales of short-term investments	1,105	1,245	1,153	3,272
Loss on disposal of variable interest entities	(186)	0	(186)	0
Other (expenses) income, net	(174)	136	(229)	(29)
<b>Total other income, net</b>	<b>2,684</b>	<b>4,017</b>	<b>4,931</b>	<b>8,276</b>
<b>(Loss) income before income tax expense (benefit), loss on equity method investment and (loss) income from discontinued operations, net of income tax</b>	<b>(280,657)</b>	<b>5,994</b>	<b>(275,467)</b>	<b>12,764</b>
<b>Income tax expense (benefit)</b>	<b>1,304</b>	<b>669</b>	<b>(5,299)</b>	<b>2,013</b>
	<b>(281,961)</b>	<b>5,325</b>	<b>(270,168)</b>	<b>10,751</b>

## Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

(Loss) income after income tax expense (benefit) before loss on equity method investment and (loss) income from discontinued operations, net of income tax				
Loss on equity method investment, net of income tax	(190)	0	(461)	0
(Loss) income from continuing operations	(282,151)	5,325	(270,629)	10,751
Discontinued operations:				
Loss from operations of discontinued operations	0	(1)	0	0
Gain on sales of discontinued operations	0	0	1,153	0
Income tax expense for discontinued operations	0	0	0	8
(Loss) income from discontinued operations, net of income tax	0	(1)	1,153	(8)
Net (loss) income	(282,151)	5,324	(269,476)	10,743
Less: Net loss attributable to noncontrolling interest	(652)	(901)	(2,078)	(1,844)
Net (loss) income attributable to AsiaInfo-Linkage, Inc.	\$ (281,499)	\$ 6,225	\$ (267,398)	\$ 12,587
Earnings per share:				
Net (loss) income from continuing operations attributable to AsiaInfo-Linkage, Inc. common stockholders:				
Basic	\$ (3.87)	\$ 0.09	\$ (3.69)	\$ 0.17
Diluted	\$ (3.87)	\$ 0.09	\$ (3.69)	\$ 0.17
Net (loss) income from discontinued operations attributable to AsiaInfo-Linkage, Inc. common stockholders:				
Basic	\$ 0.00	\$ 0.00	\$ 0.02	\$ 0.00
Diluted	\$ 0.00	\$ 0.00	\$ 0.02	\$ 0.00
Net (loss) income attributable to AsiaInfo-Linkage, Inc. common stockholders:				
Basic	\$ (3.87)	\$ 0.09	\$ (3.67)	\$ 0.17
Diluted	\$ (3.87)	\$ 0.09	\$ (3.67)	\$ 0.17
Weighted average shares used in computation:				
Basic	72,819,969	72,508,556	72,781,310	72,491,005
Diluted	72,819,969	72,763,879	72,781,310	72,744,716

See accompanying notes to condensed consolidated financial statements.

**Table of Contents****ASIAINFO-LINKAGE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)**

(U.S. dollars in thousands)

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Net (loss) income	\$ (282,151)	\$ 5,324	\$ (269,476)	\$ 10,743
Other comprehensive income (loss), net of tax:				
Change in cumulative foreign currency translation adjustment	6,656	(1,922)	7,709	(1,377)
Transfer to statements of operations of realized gain on available-for-sale securities, net of tax effects of \$166 and \$311, \$173 and \$615 for the three months and six months ended June 30, 2013 and 2012, respectively	(939)	(934)	(980)	(2,657)
Net unrealized gain on available-for-sale securities, net of tax effects of (\$41) and (\$133), (\$153) and (\$233) for the three months and six months ended June 30, 2013 and 2012, respectively	251	474	774	768
Other comprehensive income (loss)	5,968	(2,382)	7,503	(3,266)
Comprehensive (loss) income	(276,183)	2,942	(261,973)	7,477
Less: Comprehensive loss attributable to noncontrolling interest	(652)	(901)	(2,078)	(1,844)
Comprehensive (loss) income attributable to AsiaInfo-Linkage, Inc.	\$ (275,531)	\$ 3,843	\$ (259,895)	\$ 9,321

See accompanying notes to condensed consolidated financial statements.

**Table of Contents****ASIAINFO-LINKAGE, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)**

(U.S. dollars in thousands, except share and per share amounts)

	June 30, 2013	December 31, 2012
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 256,704	\$ 273,520
Restricted cash	39,435	39,639
Short-term investments available-for-sale securities	9,384	27,928
Short-term investments held-to-maturity securities	25,896	12,728
Accounts receivable (net of allowances of \$4,168 and \$2,999 as of June 30, 2013 and December 31, 2012, respectively)	341,861	285,695
Inventories, net	31,600	24,107
Other receivables	6,270	6,504
Deferred income tax assets current	5,644	5,559
Income taxes recoverable	2,496	0
Prepaid expenses and other current assets	12,695	8,311
<b>Total current assets</b>	<b>731,985</b>	<b>683,991</b>
Long-term investments	7,372	5,936
Property and equipment, net	24,756	19,104
Other acquired intangible assets, net	101,882	121,529
Deferred income tax assets non-current	2,560	2,560
Goodwill	145,453	433,545
Land use right, net	14,380	14,326
Other non-current assets	1,356	1,332
<b>Total assets</b>	<b>\$ 1,029,744</b>	<b>\$ 1,282,323</b>
<b>LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY</b>		
Current Liabilities:		
Accounts payable	\$ 112,550	\$ 78,079
Accrued expenses	22,735	28,065
Deferred revenue	37,639	40,491
Accrued employee benefits	57,304	76,803
Other payables	4,736	5,270
Income taxes payable	5,426	6,875
Other taxes payable	7,852	10,305
Deferred income tax liabilities current	1,674	1,565
<b>Total current liabilities</b>	<b>249,916</b>	<b>247,453</b>
Unrecognized tax benefits	2,477	1,703
Deferred income tax liabilities non-current	17,928	17,928
Other long term liabilities	387	387
<b>Total liabilities</b>	<b>270,708</b>	<b>267,471</b>
Redeemable noncontrolling interest	(4,885)	(3,488)

Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

Equity:

AsiaInfo-Linkage, Inc. stockholders' equity:

Common stock (100,000,000 shares authorized; \$0.01 par value; 79,030,247 shares and 78,865,818 shares issued as of June 30, 2013 and December 31, 2012, respectively; 72,863,747 shares and 72,699,318 shares outstanding as of June 30, 2013 and December 31, 2012, respectively)	790	789
Additional paid-in capital	864,371	858,711
Treasury stock, at cost (6,166,500 shares as of June 30, 2013 and December 31, 2012, respectively)	(87,746)	(87,746)
(Accumulated deficit) retained earnings	(88,340)	179,058
Statutory reserve	22,050	22,050
Accumulated other comprehensive income	52,653	45,150
 Total AsiaInfo-Linkage, Inc. stockholders' equity	 763,778	 1,018,012
 Noncontrolling interest	 143	 328
 Total equity	 763,921	 1,018,340
 Total liabilities, redeemable noncontrolling interest and equity	 \$ 1,029,744	 \$ 1,282,323

See accompanying notes to condensed consolidated financial statements.



**Table of Contents****ASIAINFO-LINKAGE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)**

(U.S. dollars in thousands)

	<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2012</b>
<b>Cash flows from operating activities:</b>		
Net (loss) income	\$ (269,476)	\$ 10,743
<b>Adjustments to reconcile net (loss) income to net cash used in operating activities:</b>		
Depreciation and amortization of property and equipment	1,169	1,800
Stock-based compensation expense	4,884	4,879
Amortization of other acquired intangible assets	19,573	20,751
Amortization of land use right	149	147
Gain on disposal of property and equipment	(68)	(209)
Gain from sales of available-for-sale securities	(1,153)	(3,272)
Loss on equity method investment	461	0
Provision of allowance for doubtful accounts	1,303	1,625
Gain on sale of discontinued operations	(1,153)	0
Loss on disposal of variable interest entities	186	0
Impairment of goodwill	286,782	0
<b>Changes in operating assets and liabilities:</b>		
Accounts receivable	(58,109)	(27,323)
Inventories	(7,493)	(5,333)
Other receivables	2,430	76
Deferred income taxes	41	(9)
Income tax recoverable	(2,496)	0
Prepaid expenses and other current assets	(4)	(1,733)
Accounts payable	34,471	5,183
Accrued expenses	(3,488)	1,871
Deferred revenue	(2,849)	2,077
Accrued employee benefits	(19,053)	(25,616)
Other payables	60	3,501
Other taxes payable	(6,834)	(3,064)
Income taxes payable	(676)	(7,445)
<b>Net cash used in operating activities</b>	<b>(21,343)</b>	<b>(21,351)</b>
<b>Cash flows from investing activities:</b>		
Decrease (increase) in restricted cash	204	(17,811)
Purchases of available-for-sale securities	0	(16,247)
Proceeds from sales of available-for-sale securities	19,893	17,936
Purchases of held-to-maturity securities	(12,947)	0
Purchases of property and equipment	(7,440)	(9,109)
Proceeds from disposal of property and equipment	16	21
Employee housing loans	(5)	0
Purchase of long-term investment	(3,051)	0
Disposal of discontinued operations	1,153	0
Disposal of variable interest entities	(857)	0
<b>Net cash used in investing activities</b>	<b>(3,034)</b>	<b>(25,210)</b>
<b>Net cash flows from financing activities:</b>		

Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

Proceeds from exercise of stock options	753	22
Increase in short-term bank loans	0	5,500
Cash provided by financing activities	753	5,522
Effect of exchange rate changes on cash and cash equivalents	6,808	(1,104)
Net decrease in cash and cash equivalents	(16,816)	(42,143)
Cash and cash equivalents at beginning of period	273,520	272,438
Cash and cash equivalents at end of period	\$ 256,704	\$ 230,295

See accompanying notes to condensed consolidated financial statements.

**Table of Contents****ASIAINFO-LINKAGE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (unaudited)**

(U.S. dollars in thousands, except share amounts)

	AsiaInfo-Linkage, Inc. Stockholders									
	Common Stock		Additional Paid-in Capital	Treasury Stock	Retained Earnings	Statutory Reserve	Accumulated Other Comprehensive Income	Total AsiaInfo-Linkage, Inc.		
	Outstanding Shares	Amount						Equity	Noncontrolling Interest	Total Equity
<b>Balance at January 1, 2012</b>	72,430,221	\$ 786	\$ 847,879	\$ (87,746)	\$ 146,527	\$ 21,748	\$ 47,124	\$ 976,318	\$ 595	\$ 976,913
Purchase of redeemable noncontrolling interest	0	0	(327)	0	0	0	0	(327)	0	(327)
Net income	0	0	0	0	32,833	0	0	32,833	(2,880)	29,953
Net loss attributable to redeemable noncontrolling interest	0	0	0	0	0	0	0	0	2,613	2,613
Statutory reserve	0	0	0	0	(302)	302	0	0	0	0
Other comprehensive loss	0	0	0	0	0	0	(1,974)	(1,974)	0	(1,974)
Stock option exercises	132,988	1	260	0	0	0	0	261	0	261
Restricted stock units vesting	136,109	2	(1)	0	0	0	0	1	0	1
Stock-based compensation (stock options)	0	0	8,077	0	0	0	0	8,077	0	8,077
Stock-based compensation (restricted stock units)	0	0	1,754	0	0	0	0	1,754	0	1,754
Excess tax benefit from stock-based compensation	0	0	1,069	0	0	0	0	1,069	0	1,069
<b>Balance at December 31, 2012</b>	72,699,318	\$ 789	\$ 858,711	\$ (87,746)	179,058	\$ 22,050	\$ 45,150	\$ 1,018,012	\$ 328	\$ 1,018,340

	AsiaInfo-Linkage, Inc. Stockholders									
	Common Stock		Additional Paid-in Capital	Treasury Stock	Retained Earnings (Accumulated deficit)	Statutory Reserve	Accumulated Other Comprehensive Income	Total AsiaInfo-Linkage, Inc.		
	Outstanding Shares	Amount						Equity	Noncontrolling Interest	Total Equity
	72,699,318	\$ 789	\$ 858,711	\$ (87,746)	\$ 179,058	\$ 22,050	\$ 45,150	\$ 1,018,012	\$ 328	\$ 1,018,340

Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

<b>Balance at January 1, 2013</b>											
Net loss	0	0	0	0	(267,398)	0	0	(267,398)	(2,078)	(269,476)	
Net loss attributable to redeemable noncontrolling interest	0	0	0	0	0	0	0	0	1,397	1,397	
Disposal of variable interest entities	0	0	0	0	0	0	0	0	496	496	
Other comprehensive income	0	0	0	0	0	0	7,503	7,503	0	7,503	
Stock option exercises	93,725	0	777	0	0	0	0	777	0	777	
Restricted stock units vesting	70,704	1	(1)	0	0	0	0	0	0	0	
Stock-based compensation (stock options)	0	0	4,010	0	0	0	0	4,010	0	4,010	
Stock-based compensation (restricted stock units)	0	0	874	0	0	0	0	874	0	874	
<b>Balance at June 30, 2013</b>	72,863,747	\$ 790	\$ 864,371	\$ (87,746)	\$ (88,340)	\$ 22,050	\$ 52,653	\$ 763,778	\$ 143	\$ 763,921	

See accompanying notes to condensed consolidated financial statements.

**Table of Contents**

**ASIAINFO-LINKAGE, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)**

**(U.S. dollars in thousands, except share and per share amounts)**

**1. BASIS OF PREPARATION**

On July 1, 2010, AsiaInfo Holdings, Inc. ( AsiaInfo ) completed its combination with internet technology ( IT ) software and solutions provider Linkage Technologies International Holdings Limited through the acquisition of 100% of the outstanding share capital of its wholly-owned subsidiary, Linkage Technologies Investment Limited ( Linkage Technologies ), and was renamed AsiaInfo-Linkage, Inc. ( AsiaInfo-Linkage ). Starting in the third quarter of 2010, AsiaInfo-Linkage s financial statements consolidated the operating results and financial position of Linkage Technologies and its consolidated subsidiaries.

(a) The accompanying unaudited condensed consolidated financial statements include the accounts of AsiaInfo-Linkage, and its subsidiaries, and its variable interest entities ( the VIEs ) (collectively, the Company ). All significant intercompany balances and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( US GAAP ) for interim financial information and with the instructions to Form 10-Q and Regulation S-X, as promulgated by the Securities and Exchange Commission. Accordingly, they do not include all of the information and notes required by US GAAP for completing annual financial statements. However, management believes that the disclosures are adequate to ensure the information presented is not misleading. US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, contingencies and results of operations. While management has based its assumptions and estimates on the facts and circumstances existing as of June 30, 2013, final amounts may differ from these estimates.

In the opinion of the management of the Company, the accompanying unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, which are necessary for a fair presentation of the results for the interim periods presented. These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s audited financial statements included in its Form 10-K for the fiscal year ended December 31, 2012. The results of operations for the interim periods presented are not indicative of the operating results to be expected for any subsequent interim period or for the Company s fiscal year ending December 31, 2013.

AsiaInfo-Linkage uses the United States ( U.S. ) dollar as its reporting currency and functional currency. The financial records of the Company s People s Republic of China ( PRC ) subsidiaries and VIEs are maintained in Renminbi ( RMB ), their functional currency and the currency of the PRC. The financial records of the Company s subsidiaries and VIEs established in Southeast Asian countries are maintained in their local currencies. Their balance sheets are translated into U.S. dollars based on the exchange rate as of the balance sheet date. Their statements of operations are translated using a weighted average exchange rate for the period. Translation adjustments are reflected in accumulated other comprehensive income in equity.

The RMB is not freely convertible into U.S. dollars or other currencies. All foreign exchange transactions involving RMB must take place through the People s Bank of China or other institutions authorized to buy and sell foreign currencies. The exchange rates adopted for foreign exchange transactions involving RMB are the rates of exchange quoted by the People s Bank of China.

No assets of the Company s consolidated VIEs are collateral for such VIEs obligations. There are no restrictions on the use of the VIEs assets to settle the Company s obligations. As of June 30, 2013 and December 31, 2012, respectively, there were \$0 and \$3,222 of liabilities of the Company s consolidated VIEs for which creditors (or beneficial interest holders) did not have recourse to the general credit of AsiaInfo-Linkage or its subsidiaries.

---

## **Table of Contents**

(b) The accompanying unaudited condensed consolidated financial statements have been prepared using the same accounting policies as used in the preparation of the Company's consolidated financial statements on Form 10-K for the fiscal year ended December 31, 2012.

### **Disposal of Variable Interest Entities**

The Company and its two consolidated VIEs in China, Beijing Zhongxinjia Sci-Tech Development Co., Ltd. ( ZXJ ) and Beijing Star VATS Technologies Co., Inc. ( Beijing Star VATS ) entered into a series of agreements in May 2013. Pursuant to these agreements, the Company transferred its interests in the VIEs, in exchange for payments secured by a charge over and pledge of the interests in the VIEs in favor of the Company. As a result of these agreements, the Company no longer holds a controlling financial interest in the VIEs. The disposal loss recognized in the second quarter of 2013 was \$186.

### **Accounting Pronouncements**

#### *Newly adopted accounting pronouncements*

In December 2011, the Financial Accounting Standard Board (the FASB ) issued an authoritative pronouncement related to disclosures about offsetting assets and liabilities. The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. In January 2013, the FASB further clarifies that ordinary trade receivables and receivables are not in the scope of the authoritative pronouncement and the pronouncement applies only to derivatives, repurchase agreements and reverse purchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria contained in the FASB Accounting Standards Codification or subject to a master netting arrangement or similar agreement. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The adoption of this guidance did not have a significant effect on the Company's consolidated financial statements.

In February 2013, the FASB issued an authoritative pronouncement related to reporting of amounts reclassified out of accumulated other comprehensive income, to improve the transparency of reporting these reclassifications. Other comprehensive income includes gains and losses that are initially excluded from net income for an accounting period. Those gains and losses are later reclassified out of accumulated other comprehensive income into net income. The guidance does not change the current requirements for reporting net income or other comprehensive income in financial statements.

The guidance will require an organization to:

Present (either on the face of the statement where net income is presented or in the notes) the effects on the line items of net income of significant amounts reclassified out of accumulated other comprehensive income but only if the item reclassified is required under US GAAP to be reclassified to net income in its entirety in the same reporting period.

Cross-reference to other disclosures currently required under US GAAP for other reclassification items (that are not required under US GAAP) to be reclassified directly to net income in their entirety in the same reporting period. This would be the case when a portion of the amount reclassified out of accumulated other comprehensive income is initially transferred to a balance sheet account (e.g., inventory for pension-related amounts) instead of directly to income or expense.

## **Table of Contents**

The guidance applies to all public and private companies that report items of other comprehensive income. Public companies are required to comply with the guidance for all reporting periods (interim and annual) effective for reporting periods beginning after December 15, 2012. Early adoption is permitted. The Company has adopted this guidance on January 1, 2013 and has presented the relevant details in the notes to the financial statements.

### ***Recent accounting pronouncements not yet adopted***

In February 2013, the FASB issued an authoritative pronouncement related to obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed at the reporting date. The guidance addresses the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this pronouncement is fixed at the reporting date, except for obligations addressed within existing guidance in US GAAP. The guidance requires an entity to measure those obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance also requires an entity to disclose the nature and amount of the obligation as well as other information about those obligations. The guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. The guidance should be applied retrospectively to all prior periods presented for those obligations resulting from joint and several liability arrangements within the scope that exist at the beginning of an entity's fiscal year of adoption. An entity may elect to use hindsight for the comparative periods (if it changed its accounting as a result of adopting the guidance in this pronouncement) and should disclose that fact. Early adoption is permitted. The Company is in the process of evaluating the effect of adoption of this guidance on the Company's consolidated financial statements.

In March 2013, the FASB issued an authoritative pronouncement related to parent's accounting for the cumulative translation adjustment upon derecognition of certain subsidiaries or groups of assets within a foreign entity or of an investment in a foreign entity. When a reporting entity (parent) ceases to have a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business (other than a sale of in substance real estate or conveyance of oil and gas mineral rights) within a foreign entity, the parent is required to release any related cumulative translation adjustment into net income. Accordingly, the cumulative translation adjustment should be released into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided.

For an equity method investment that is a foreign entity, the partial sale guidance still applies. As such, a pro rata portion of the cumulative translation adjustment should be released into net income upon a partial sale of such an equity method investment. However, this treatment does not apply to an equity method investment that is not a foreign entity. In those instances, the cumulative translation adjustment is released into net income only if the partial sale represents a complete or substantially complete liquidation of the foreign entity that contains the equity method investment.

Additionally, the guidance clarifies that the sale of an investment in a foreign entity includes both: (1) events that result in the loss of a controlling financial interest in a foreign entity (i.e., irrespective of any retained investment); and (2) events that result in an acquirer obtaining control of an acquiree in which it held an equity interest immediately before the acquisition date (sometimes also referred to as a step acquisition). Accordingly, the cumulative translation adjustment should be released into net income upon the occurrence of those events.

The guidance is effective prospectively for fiscal years (and interim reporting periods within those years) beginning after December 15, 2013. The guidance should be applied prospectively to derecognition events occurring after the effective date. Prior periods should not be adjusted. Early adoption is permitted. If an entity elects to early adopt the guidance, it should apply the guidance as of the beginning of the entity's fiscal year of adoption. The Company is in the process of evaluating the effect of adoption of this guidance on the Company's consolidated financial statements.

**Table of Contents**

In July 2013, the FASB issued a pronouncement which provides guidance on financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists.

The guidance states that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets.

The guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. Early adoption is permitted. The guidance should be applied prospectively to all unrecognized tax benefits that exist at the effective date. Retrospective application is permitted. The Company is in the process of evaluating the effect of adoption of this guidance on the Company's consolidated financial statements.

**2. FINANCIAL INSTRUMENTS**

Financial instruments consist of cash and cash equivalents, restricted cash, short-term investments, accounts receivable, other receivables, accounts payable, accrued expenses, other payables, income taxes payable and recoverable, other taxes payable and long-term investments.

Short-term investments are classified as available-for-sale securities and held-to-maturity securities, as discussed in Note 4. Certain long-term investments have been written down to their fair value, as discussed in Note 7. Fair value of other long-term investments is not disclosed because the fair value of the investments is not readily determinable.

The carrying values of other financial instruments approximate their fair values due to the short-term nature of these instruments. The Company does not use derivative instruments to manage risks.

**3. CASH AND CASH EQUIVALENTS**

Cash and cash equivalents consist of cash on hand, demand deposits and highly liquid investments, which are unrestricted as to withdrawal or use, and which have remaining maturities of three months or less when purchased. The following table provides additional information concerning the breakdown of the Company's cash and cash equivalents:

	<b>June 30, 2013</b>	<b>December 31, 2012</b>
Cash	\$ 99,565	\$ 101,642
Cash equivalents:		
Money market funds	123,961	148,332
Others	33,178	23,546
<b>Total cash and cash equivalents</b>	<b>\$ 256,704</b>	<b>\$ 273,520</b>

**4. SHORT-TERM INVESTMENTS**

Short-term investments consist of available-for-sale securities and held-to-maturity securities. As of June 30, 2013 and December 31, 2012, the Company did not hold trading securities.

As of June 30, 2013 and December 31, 2012, the Company's held-to-maturity securities were carried at cost of \$25,896 and \$12,728, respectively. The held-to-maturity securities are either not allowed to be redeemed early or are subject to penalty for early redemption before their maturity. The carrying amounts of the held-to-maturity securities approximate their fair values due to their short-term nature, which are within one-year maturity period.





**Table of Contents**

The following table provides additional information concerning the Company's available-for-sale securities, which consist principally of bond funds and corporate convertible notes issued by major financial institutions or companies. The available-for-sale securities have no contractual maturity dates and the Company can sell the investments at any time at the Company's decision.

	June 30, 2013				December 31, 2012			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair value	Cost	Gross unrealized gains	Gross unrealized losses	Fair value
Bond funds	\$ 8,672	\$ 712	\$ 0	\$ 9,384	\$ 26,090	\$ 938	\$ 0	\$ 27,028
Corporate convertible notes	0	0	0	0	900	0	0	900
<b>Total</b>	<b>\$ 8,672</b>	<b>\$ 712</b>	<b>\$ 0</b>	<b>\$ 9,384</b>	<b>\$ 26,990</b>	<b>\$ 938</b>	<b>\$ 0</b>	<b>\$ 27,928</b>

The following table provides additional information on the realized gains of the sale of available-for-sale securities during the three-month and six-month periods ended June 30, 2013 and 2012, respectively. For purposes of determining gross realized gains, the cost of securities sold is based on specific identification.

	Three Months Ended June 30,					
	2013			2012		
	Proceeds	Costs	Gains	Proceeds	Costs	Gains
Available-for-sale securities	\$ 17,353	\$ 16,248	\$ 1,105	\$ 7,362	\$ 6,117	\$ 1,245
<b>Total</b>	<b>\$ 17,353</b>	<b>\$ 16,248</b>	<b>\$ 1,105</b>	<b>\$ 7,362</b>	<b>\$ 6,117</b>	<b>\$ 1,245</b>

	Six Months Ended June 30,					
	2013			2012		
	Proceeds	Costs	Gains	Proceeds	Costs	Gains
Available-for-sale securities	\$ 19,893	\$ 18,740	\$ 1,153	\$ 17,936	\$ 14,664	\$ 3,272
<b>Total</b>	<b>\$ 19,893</b>	<b>\$ 18,740</b>	<b>\$ 1,153</b>	<b>\$ 17,936</b>	<b>\$ 14,664</b>	<b>\$ 3,272</b>

The Company reported no impairment loss for its short-term investments for the three-month and six-month periods ended June 30, 2013 or 2012.

**5. ACCOUNTS RECEIVABLE**

Accounts receivable balances included both billed and unbilled amounts. Revenue recognized in excess of billings is recorded as unbilled receivables. All billed and unbilled amounts are expected to be collected within one year. Accounts receivable balances included bank acceptance drafts receivable and commercial acceptance drafts receivable. These bank acceptance drafts and commercial acceptance drafts were non-interest bearing and were due within six months of issuance.

**Table of Contents**

The Company generated service revenues by acting as a sales agent for International Business Machines Corporation ( IBM ) or its distributors, and for a few other hardware companies, for certain products sold to the customers of the Company (each, an IBM-Type Arrangement ). The components of the Company's accounts receivable as of June 30, 2013 and December 31, 2012, including amounts attributable to the IBM-Type Arrangements, were as follows:

	June 30, 2013			December 31, 2012		
	IBM-Type Arrangement	Non-IBM-Type Arrangement	Total	IBM-Type Arrangement	Non-IBM-Type Arrangement	Total
Billed accounts receivable	\$ 42,037	\$ 99,423	\$ 141,460	\$ 17,656	\$ 87,830	\$ 105,486
Unbilled accounts receivable	43,560	154,876	198,436	37,069	141,993	179,062
Bank acceptance drafts	0	373	373	0	1,684	1,684
Commercial acceptance drafts	0	5,760	5,760	0	2,462	2,462
Less: allowance for doubtful accounts	(142)	(4,026)	(4,168)	(291)	(2,708)	(2,999)
Total accounts receivable, net	\$ 85,455	\$ 256,406	\$ 341,861	\$ 54,434	\$ 231,261	\$ 285,695

**6. INVENTORIES, NET**

The components of inventories, net as of June 30, 2013 and December 31, 2012 were as follows:

	June 30, 2013	December 31, 2012
Deferred costs	\$ 13,680	\$ 10,857
Finished goods	17,920	13,250
<b>Total</b>	<b>\$ 31,600</b>	<b>\$ 24,107</b>

Deferred costs represent the costs incurred for the implementation phases of the projects outside of China, which provide multiple services and products (software, hardware, implementation, maintenance and managed services) to customers and include around 1-2 years system implementation periods. The deferred costs are to be reimbursed after the successful launch of the system, and were capitalized as inventories and expected to be transferred to cost of revenues upon revenue recognition.

**7. LONG-TERM INVESTMENTS**

(a) In October 2005, the Company acquired five percent of the outstanding equity interests of Hinge. The investment is accounted for using the cost method as the Company does not have a significant influence over the business and operations of Hinge. Due to the effects of the global financial crisis in 2008, Hinge's business dropped significantly during 2008 causing a significant decline in fair value of Hinge. The Company determined that its investment in Hinge became worthless as of December 31, 2008 and that the decline in the fair value was other-than-temporary. Consequently, the Company recognized an impairment loss of \$2,042, which is equal to the carrying amount of the investment after foreign exchange adjustment from the initial investment cost.

(b) On September 12, 2008, the Company acquired 2,170,000 redeemable convertible Series B Preferred Shares of C-Platform Corporation ( C-Platform ), for a total cash consideration of \$4,696, including \$52 in transaction costs. The total consideration had been paid as of September 30, 2008. Following the transaction, the Company owned approximately 19.9% of C-Platform's issued and outstanding share capital, or 17% of C-Platform's share capital on a fully-diluted basis. In August 2009 and March 2011, the Company paid for and acquired \$167 and \$409 of convertible promissory notes from C-Platform, respectively. Such convertible promissory notes were accounted for as a short-term investment, available-for-sale securities. In March 2011, the Company converted \$167 of the convertible promissory notes into 78,023 of C-Platform's Series B Preferred Shares, which were accounted for as a long-term investment, and obtained the share certificate in July 2011, while \$409 of convertible promissory notes remained unconverted. Following the transaction, the Company owned approximately 19.61% of C-Platform's issued and outstanding share capital. In February 2012, the Company converted the remaining \$409 of convertible promissory notes into 191,008 of C-Platform's Series B Preferred Shares, which were accounted for as a long-term investment, and obtained the share certificate in April 2012. Following the transaction, the Company owned approximately 18.63% of C-platform's issued and outstanding shares. Because the

## Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

Company does not have the ability to exercise significant influence over the operating and financial policies of C-Platform, the Company uses the cost method of accounting to record its investment in C-Platform.

**Table of Contents**

C-Platform is a Cayman Islands company, which, through its subsidiaries in China, provides data operating services, a form of value-added telecommunication services, to telecommunications carriers in China. The Company believes that the transaction furthers its ongoing strategy of expanding its market leading telecommunications software solutions business in China.

(c) On November 30, 2010, the Company acquired 3,562,500 Series A-1 Preferred Shares of Santen Corporation ( Santen ), for a total cash consideration of \$950 for 9.5% of Santen s issued and outstanding voting share capital. Since the Company does not have the ability to exercise significant influence over the operating and financial policies of Santen, the Company uses the cost method of accounting to record its investment in Santen.

Santen is a Cayman Islands company, which, through its subsidiaries in China, provides a form of value-added telecommunication services, to telecommunications carriers in China. In 2011, the Company performed an assessment of the financial condition of Santen and determined there was an other-than-temporary decline of fair value. Based on the assessment, the Company provided for an impairment loss of \$950, which is equal to the carrying amount of the investment.

(d) On June 20, 2012, Beijing Star VATS entered into an investment agreement with Beijing Naomi Technology Limited ( Naomi ), which provides personalized internet-based product recommendations based on customers on-line purchasing patterns. Pursuant to the investment agreement, Beijing Star VATS agreed to invest \$1,898 in Naomi in two tranches. The first tranche totaling \$947 was paid to Naomi in July 2012. The second tranche totaling \$951 was paid to Naomi in April 2013.

The Company has adopted the equity method to recognize the investment as the Company, which holds a 40% voting interest in Naomi, is able to exercise significant influence over the operating and financial policies of Naomi. The Company has recognized a loss on equity method investment in the amount of \$190 and \$461 for the three-month and six-month period ended Jun 30, 2013, respectively.

In May 2013, the Company disposed of its long-term investment in Naomi following the disposal of Beijing Star VATS.

(e) On January 28, 2013, the Company acquired 9,566,716 Series A-1 Preferred Shares of GEO Holdings Ltd.( GEO ), for a total cash consideration of \$2,100 representing a 6.89% of GEO s issued and outstanding voting share capital. Since the Company does not have the ability to exercise significant influence over the operating and financial policies of GEO, the Company uses the cost method of accounting to record its investment in GEO.

**8. GOODWILL**

The changes in the carrying amount of goodwill during the six months ended June 30, 2013 were as follows:

	<b>Amount</b>
<b>Gross amount:</b>	
Beginning balance at January 1, 2013:	\$ 460,045
Disposal of variable interest entities	(1,448)
Exchange differences	147
<b>Ending balance at June 30, 2013:</b>	<b>458,744</b>
<b>Accumulated impairment loss:</b>	
Beginning balance at January 1, 2013:	(26,500)
Impairment of goodwill	(286,782)
Exchange differences	(9)
<b>Ending balance at June 30, 2013:</b>	<b>(313,291)</b>
<b>Goodwill, net at June 30, 2013</b>	<b>\$ 145,453</b>



**Table of Contents**

In the second quarter of 2013, the Company's operating environment began to deteriorate as evidenced by a decrease in current and projected growth rates for the China gross domestic product, compared to historical growth rates, and continued uncertainty of government policies for the telecommunications and internet industries which changed market participant valuation assumptions including discount rates. On May 12, 2013, upon the unanimous recommendation of the Special Committee of its Board of Directors and the approval of its Board of Directors, the Company entered into a definitive agreement under which the Company would be acquired by an investor consortium led by CITIC Capital Partners, a director of the Company and their respective affiliates. Under the terms of the definitive agreement, the Company was valued at approximately \$896,700. In management's judgement, the valuation represented the fair value of the Company's reporting unit in assessing goodwill impairment considering the aforementioned factors. Because the fair value of the reporting unit was less than its carrying amount, the Company performed the second step of the interim test for goodwill impairment in the second quarter of 2013.

The Company performed the second step of the impairment test to determine the implied fair value of goodwill for the reporting unit, which requires management to allocate the fair value of the reporting unit to all of the assets and liabilities including any unrecognized intangible assets of the reporting unit.

Based on the results of the impairment test, the Company recognized a loss on impairment of goodwill of \$286,782 in the three months ended June 30, 2013.

**Table of Contents****9. OTHER ACQUIRED INTANGIBLE ASSETS, NET**

The carrying amounts of the components of other acquired intangible assets, net as of June 30, 2013 and December 31, 2012 were as follows:

	June 30, 2013				Net carrying amount	December 31, 2012			
	Gross carrying amount	Accumulated amortization	Disposal of VIE	Foreign exchange difference		Gross carrying amount	Accumulated amortization	Foreign exchange difference	Net carrying amount
Core technologies	\$ 45,931	\$ (24,131)	\$ 0	\$ 0	\$ 21,800	\$ 45,931	\$ (20,498)	\$ 0	\$ 25,433
Trade names and trademarks	21,037	(3,604)	0	0	17,433	21,037	(3,059)	0	17,978
Contract backlogs	12,474	(12,486)	0	12	0	12,474	(12,480)	12	6
Customer lists	131	(143)	0	12	0	131	(143)	12	0
Customer relationships	117,755	(55,895)	0	311	62,171	117,755	(47,287)	311	70,779
Distribution networks	870	(870)	0	0	0	870	(870)	0	0
Software	1,721	(1,884)	0	163	0	1,721	(1,884)	163	0
Non-compete agreements	1,249	(913)	0	25	361	1,249	(810)	25	464
Corporate business agency agreements	2,037	(1,956)	(75)	6	12	2,037	(1,695)	5	347
Existing technology	38,500	(38,395)	0	0	105	38,500	(31,978)	0	6,522
	\$ 241,705	\$ (140,277)	\$ (75)	\$ 529	\$ 101,882	\$ 241,705	\$ (120,704)	\$ 528	\$ 121,529

The future amortization expenses for the net carrying amount of intangible assets with definite lives as of June 30, 2013 are expected to be as follows:

Six-month period ended December 31, 2013	\$ 12,956
2014	23,469
2015	21,110
2016	14,950
2017 and thereafter	29,397
	\$ 101,882

**10. LAND USE RIGHT, NET**

From 2009, the Company completed the process to obtain a land use right for a piece of land in Beijing, on which the Company plans to construct a building for use as its new corporate headquarters. In October 2009, the Company entered into an agreement with Zhongguancun Software Park Development Co., Ltd. ( ZSPD ), pursuant to which ZSPD agreed to develop the land in preparation for construction of the building, for an aggregate consideration of approximately \$10,777, of which \$10,000 was paid in years 2009 and 2010 and \$777 was paid in 2011.

In connection with the agreement with ZSPD, the Company became eligible to enter into a land transfer agreement with relevant PRC government authorities in order to obtain the land use right with respect to such land. In May 2011, the Company entered into a land use right transfer agreement with the Beijing Municipal Bureau of Land and Resources pursuant to which the Company would acquire the land use right with a 50-year term, for a consideration of approximately \$2,870, plus related local levy of \$111, paid in June and August 2011, respectively.

In respect of these agreements, the Company has recorded the aggregate amount of the consideration paid, amounting to \$14,739 after an exchange rate effect of \$981, as a payment for land use right. In November 2011, the Company obtained the National Land Use Right Certificate, issued by the Beijing Municipal Bureau of Land and Resources, and accordingly the Company records the payment for land use right at cost less accumulated amortization and amortizes the cost of the land use right on a straight-line basis over the 50-year term of the land use right certificate. As of June 30, 2013, the land use right amounted to \$14,380, which was the cost less the accumulated amortization of \$639 and



plus an exchange rate gain of \$280.

## **Table of Contents**

### **11. OTHER NON-CURRENT ASSETS**

In 2012, the Company launched an employee housing loan program which provides non-interest bearing loans to qualified employees with a five-year term. As of June 30, 2013 and December 31, 2012, the total amount of loans granted under the program was \$1,616 and 1,611, respectively, and the loans due in more than one year classified in other non-current assets were \$1,356 and 1,332, respectively.

### **12. ACCOUNTS PAYABLE**

Accounts payable included bank acceptance drafts payable of \$2,053 and \$3,427, and commercial acceptance drafts payable of \$0 and \$139 as of June 30, 2013 and December 31, 2012, respectively. These bank acceptance drafts and commercial acceptance drafts were non-interest bearing and were due within six months of issuance.

As of June 30, 2013 and December 31, 2012, the Company's accounts payable balance related to the IBM-Type Arrangements was \$87,842 and \$63,148, respectively, under which the Company is contractually obligated to pay its vendors only when its customers pay the Company.

### **13. CREDIT FACILITIES**

As of June 30, 2013, the Company had credit facilities for working capital purposes totaling \$152,062 expiring on various dates up to April 2014, which were secured by bank deposits of \$33,938. As of June 30, 2013, unused credit facilities were \$124,263 and used credit facilities totaled \$27,799. The credit facilities were used to cover issuance of standby letters of credit for customers, borrowing of short-term bank loans and issuance of bank acceptance drafts payable to hardware suppliers.

As of December 31, 2012, the Company had credit facilities for working capital purposes totaling \$150,480 expiring on various dates up to March 2014, which were secured by bank deposits of \$33,482. As of December 31, 2012, unused credit facilities were \$122,802 and used credit facilities totaled \$27,678. The credit facilities were used to cover issuance of standby letters of credit to customers, borrowing of short-term bank loans and issuance of bank acceptance drafts payable to hardware suppliers.

In addition to the bank deposits pledged for the above credit facilities, the Company also collateralized bank deposits of \$5,497 and \$6,157 for the issuance of certain standby letters of credit and bank acceptance drafts, as of June 30, 2013 and December 31, 2012, respectively. Therefore, total bank deposits of \$39,435 and \$39,639 were presented as restricted cash in the consolidated balance sheets as of June 30, 2013 and December 31, 2012, respectively.

### **14. VALUE-ADDED TAXES REBATE**

Revenue from software products and solutions included the benefit of the rebate of value-added taxes on sales of software and services as part of the PRC government's policy of encouraging software development in the PRC. The rebate totaled \$3,297 and \$4,065 for the six months ended June 30, 2013 and 2012, respectively.

### **15. INCOME TAXES**

The Company is subject to U.S. federal and state income taxes and the Company's subsidiaries and VIEs incorporated in the PRC are subject to PRC income taxes.

**Table of Contents**

Reconciliation between the provision for income taxes expenses (benefit) from continuing operation computed by applying the U.S. federal tax rate to (loss) income before income taxes and the actual provision for income taxes was as follows:

	Six Months Ended June 30,	
	2013	2012
U.S. federal rate	35%	35%
Difference between statutory rate and foreign effective tax rate	(25%)	(29%)
Subpart F income inclusion and other dividend income	4%	6%
Stock-based compensation	3%	5%
Tax effect due to reduced rate granted for 2011 and 2012	(73%)	0%
Impairment of goodwill	48%	0%
Change in valuation allowance	15%	0%
Effect of change in repatriation of foreign earnings of certain subsidiaries	5%	0%
Non-deductible meals and entertainment expenses	3%	0%
PRC super research and development deduction	(4%)	0%
True-up of China tax returns	(4%)	0%
Others	(5%)	(1%)
	2%	16%

The tax rate for the six months ended June 30, 2013 was lower than that of the same period in 2012 mainly because two of the Company's subsidiaries, AsiaInfo-Linkage Technologies (China), Inc. ( AIBJ ) and Linkage-AsiaInfo Technologies (Nanjing), Inc., ( Linkage Nanjing ) recognized the tax benefit of 2011 and 2012 Key Software Enterprise ( KSE ) status in the first quarter of 2013. Pursuant to the relevant rules, a company with KSE status could apply a reduced income tax rate of 10%. These entities applied for this status for 2011 and 2012 and received approvals in the first quarter of 2013. Thus, the tax benefit was reflected in the three months ended March 31, 2013. Total income taxes recoverable related to reduced income tax rate granted was \$2,496 as of June 30, 2013.

Aggregate undistributed earnings of approximately \$40,018 on June 30, 2013 of the Company's PRC subsidiaries and VIEs that were available for distribution to the Company are considered to be indefinitely reinvested under US GAAP and, accordingly, no provision has been made for the Chinese withholding taxes on dividends that would be payable upon the distribution of those amounts to AsiaInfo-Linkage. Additionally, the Chinese tax authorities have clarified that distributions to be made out of retained earnings from prior to January 1, 2008 would not be subject to the Chinese withholding tax. Determination of the amount of any unrecognized deferred income tax liabilities on those earnings is not practicable.

The Company is subject to taxation in the U.S. and various states and foreign jurisdictions. There is no ongoing examination by any tax authority at this time. The Company did not change its position regarding recognition of uncertain tax benefit in the six months ended June 30, 2013, the movement in the unrecognized tax benefit was mainly due to the true up with relevant to AIBJ's rate change for 2011 and 2012. The Company's various tax years from 2003 to 2012 remain open in these taxing jurisdictions.

**16. STOCK-BASED COMPENSATION*****2002 Stock Option Plan and Prior Plans***

Under the Company's 2002 Stock Option Plan (the 2002 Plan ), the Company was authorized to grant options for the purchase of up to 4,500,000 shares of common stock to employees, directors and consultants at prices not less than the fair market value on the date of grant for incentive stock options and nonqualified options. Shares as to which an option is granted under the 2002 Plan but remains unexercised at the expiration, forfeiture or other termination of such option may be the subject of the grant of further options. Prior to adopting the 2002 Plan, the Company adopted annual stock option plans for each of 1995, 1996, 1997, 1998, 1999 and 2000 (such plans, together with the 2002 Plan, are referred to hereinafter as the Option Plans ).

**Table of Contents**

The vesting periods of the options under the Option Plans are determined based on individual stock option agreements. Options granted prior to 1998 generally vested and became exercisable over three years at an equal annual rate. Exercise terms of options granted in 1998, 1999, 2000 and 2002 are substantially similar to those of options granted prior to 1998 except that the vesting and exercise periods were generally over four years at an annual rate of 20%, 20%, 30% and 30% for the 1999 plan and were generally over four year cliffs at an annual rate of 25% for the 2000 plan, and are generally no more than four years at an annual rate of 25% from the date of grant for the 2002 Plan.

The Option Plans as of June 30, 2013 and activities during the six months ended June 30, 2013 were as follows:

	Number of shares	Weighted average exercise price per share	Aggregate intrinsic value
Outstanding, January 1, 2013	200,248	\$ 5.41	
Forfeited	(500)	3.42	
Exercised	(2,582)	5.21	
Outstanding, March 31, 2013	197,166	\$ 5.42	\$ 1,272
Exercised	(8,325)	6.55	
Outstanding, June 30, 2013	188,841	\$ 5.37	\$ 1,165
Exercised and expected to exercise, June 30, 2013	188,841	5.37	1,165
Exercisable, June 30, 2013	188,841	\$ 5.37	1,165

The aggregate intrinsic value was calculated as the difference between the exercise price of the underlying awards and the closing stock price of \$11.54 per share of the Company's common stock on the last trading day in the Company's second fiscal quarter of 2013 (June 28, 2013).

Total intrinsic value of options exercised for each of the three months ended June 30, 2013 and 2012 was \$42 and \$20, respectively.

As of June 30, 2013, although there was no unrecognized stock-based compensation cost relating to the Option Plans, the Option Plans still had unexercised options, which are expected to be exercised over a weighted-average vesting period of 1.02 years.

**2005 Stock Incentive Plan - Restricted Stock Units (RSUs)**

Under the 2005 Stock Incentive Plan (the 2005 Plan), the Company was authorized to grant participants restricted stock units, stock options, or other types of equity incentives. The number of shares authorized for issuance was (a) 600,000 shares plus (b) any authorized shares of common stock that, as of April 21, 2005, were available for issuance under the Company's 2002 Stock Option Plan, or that thereafter became available for issuance under the 2002 Plan in accordance with its terms.

An RSU is an agreement to issue stock at the time the award vests. These units vest on an annual basis equally over four years, 25% on each anniversary of the grant date. The fair value of each RSU is measured on the grant date based on the market price of the stock on the grant date. The Company also has the right at its sole discretion to pay cash in lieu of the issuance of vested shares of common stock. No such cash payment right was exercised by the Company.

**Table of Contents**

RSUs under the 2005 Plan as of June 30, 2013 and activities during the six months ended June 30, 2013 were as follows:

	Number of shares	Weighted average grant date fair value per share
Restricted stock units unvested at January 1, 2013	41,850	\$ 22.60
Vested	(10,700)	24.52
Restricted stock units unvested at March 31, 2013	31,150	\$ 21.95
Vested	(3,000)	19.44
Restricted stock units unvested at June 30, 2013	28,150	\$ 22.21

Total intrinsic values of RSUs vested for the three months ended June 30, 2013 and 2012 were \$35 and \$32, respectively.

As of June 30, 2013, there was \$367 of unrecognized stock-based compensation cost related to RSUs, which is expected to be recognized into the consolidated statements of operations over a weighted-average vesting period of 0.65 years. To the extent the actual forfeiture rate is different from the original estimate, the stock-based compensation cost related to these awards may be different from the expectation.

***2008 Stock Incentive Plan Performance-based Restricted Stock Units (PSUs)***

On February 25, 2008, the Board of Directors of the Company authorized the 2008 Stock Incentive Plan, as amended (the 2008 Plan). The 2008 Plan was subsequently approved by the Company's stockholders at the 2008 annual meeting of stockholders. Under the 2008 Plan, the Company may grant participants restricted stock awards, stock options, or other types of equity incentives. The number of shares authorized for issuance is (a) 2,000,000 shares plus (b) any authorized shares of the Company's common stock that, as of February 25, 2008, were available for issuance under the Company's 2005 Plan, or that thereafter become available for issuance under the 2005 Plan in accordance with its terms.

As of June 30, 2013, an aggregate of 1,689,400 PSUs granted under the 2008 Plan had fully vested based on certain performance criteria or been forfeited.

***2011 Stock Incentive Plan***

In February 2011, the Board of Directors of the Company authorized the 2011 Stock Incentive Plan (the 2011 Plan). The 2011 Plan was subsequently approved by the Company's stockholders on April 21, 2011 at the 2011 annual meeting of stockholders. Under the 2011 Plan, the Company is authorized to grant participants restricted stock awards, stock options, or other types of equity incentives. The number of shares authorized for issuance was (a) 7,501,752 shares plus (b) any authorized shares of the Company's common stock that, as of April 21, 2011, were available for issuance under the 2008 Plan, or that thereafter become available for issuance under the 2008 Plan in accordance with its terms.

***RSUs under 2011 Plan***

As of June 30, 2013, 235,367 RSUs were granted under the 2011 Plan. Each RSU represents a contingent right to receive one share of common stock. Some awards vest in two equal installments on the 6-month and 12-month anniversaries of the grant date, and the other awards vest on annual basis equally over four years, 25% on each anniversary of the grant date. The fair value of each RSU is measured on the grant date based on the market price of the stock on the grant date. The Company also has the right, in its sole discretion, to pay cash in lieu of the issuance of vested shares of common stock. No such cash payment right was exercised by the Company.

**Table of Contents**

RSUs under the 2011 Plan as of June 30, 2013 and activities during the six months ended June 30, 2013 were as follows:

	Number of shares	Weighted average grant date fair value per share
Restricted stock units unvested at January 1, 2013	137,758	\$ 12.86
Vested	(47,379)	10.92
Restricted stock units unvested at March 31, 2013	90,379	\$ 13.88
Vested	(9,625)	18.80
Restricted stock units unvested at June 30, 2013	80,754	\$ 13.30

The total intrinsic value of RSUs vested for the three months ended June 30, 2013 and 2012 was \$112 and \$101, respectively.

As of June 30, 2013, there was \$582 of unrecognized stock-based compensation cost related to RSUs, which is expected to be recognized into the consolidated statements of operations over a weighted-average vesting period of 0.62 years. To the extent the actual forfeiture rate is different from original estimate, actual stock-based compensation related to these awards may be different from these expectations.

In December 2011, the Compensation Committee of the Board of Directors of the Company, pursuant to the 2011 Plan, approved grants of stock options to the Company's executive officers and employees.

**Stock Options under 2011 Plan**

Stock options under 2011 Plan as of June 30, 2013 and activities during the six months ended June 30, 2013 were as follows:

	Number of shares	Weighted average exercise price per share	Aggregate intrinsic value
Outstanding, January 1, 2013	6,467,950	\$ 8.84	
Granted	28,000	11.02	
Exercised	(20,475)	8.73	
Forfeited	(43,650)	8.73	
Outstanding, March 31, 2013	6,431,825	\$ 8.85	\$ 19,550
Granted	32,000	11.81	
Exercised	(84,175)	8.73	
Forfeited	(67,650)	8.73	
Outstanding, June 30, 2013	6,312,000	\$ 8.86	\$ 17,037
Exercised and expected to exercise, June 30, 2013	6,312,000	8.86	17,037
Exercisable, June 30, 2013	1,364,110	\$ 8.81	3,748

The aggregate intrinsic value was calculated as the difference between the exercise price of the underlying awards and the closing stock price of \$11.54 per share of the Company's common stock on the last trading day in the Company's second fiscal quarter of 2013 (June 28, 2013).

Total intrinsic value of options exercised for the three months ended June 30, 2013 and 2012 was \$190 and nil, respectively.

## Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

As of June 30, 2013, there was \$23,711 of unrecognized stock-based compensation cost relating to the 2011 Plan, which is expected to be exercised over a weighted-average vesting period of 8.47 years. To the extent the actual forfeiture rate is different from original estimate, actual stock-based compensation related to these awards may be different from these expectations.

**Table of Contents**

The amount of stock-based compensation attributable to cost of revenues, sales and marketing, general and administrative expenses, and research and development is included in those line items in the accompanying consolidated statements of operations. For the three months and six months ended June 30, 2013 and 2012, stock-based compensation expense related to the stock options and stock units were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Cost of revenues	\$ 803	\$ 816	\$ 1,638	\$ 1,667
Sales and marketing	600	612	1,220	1,202
General and administrative	770	727	1,490	1,411
Research and development	267	299	536	599
<b>Total stock-based compensation expenses</b>	<b>\$ 2,440</b>	<b>\$ 2,454</b>	<b>\$ 4,884</b>	<b>\$ 4,879</b>

**17. FAIR VALUE MEASUREMENTS**

*Measured on recurring basis*

The Company measured the cash equivalents and the short-term investments available-for-sale securities at fair value on a recurring basis as of June 30, 2013 and December 31, 2012.

Cash equivalents are classified within Level 1 of the fair value hierarchy because they are valued based on the quoted market price in an active market.

The Company uses quoted prices in active markets for identical assets (Level 1 investments) to determine the fair value of available-for-sale securities. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then the Company uses quoted prices for similar assets and liabilities or inputs other than the quoted prices that are observable either directly or indirectly, which are included in Level 2 investments.

The Company did not have Level 2 investments as of June 30, 2013 and December 31, 2012.

The Company did not have Level 3 investments as of June 30, 2013. The Level 3 investments as of December 31, 2012 were convertible promissory notes issued by GEO. The notes bore an annual interest rate of 8% after 90 days of the issuing date, and were due and payable to the purchaser or convertible into shares of GEO's Series A Preferred Shares or other similar equity securities, upon execution of securities purchase and sales agreements.

As the convertible notes were issued by a private company and not traded on any market, in determining the fair value of the Level 3 investments, the Company used the principal amount of the investments, and the interest accrued on a quarterly basis after 90 days of the issuing date. The Company also considered the credit risk related to the issuer. The Company believes this method provided a reasonable fair value of the investments.

The available-for-sale securities measured and recorded at fair value as of June 30, 2013 and December 31, 2012 were as follows:

June 30, 2013 Fair Value Measurements at the Reporting Date				December 31, 2012 Fair Value Measurements at the Reporting Date			
Using				Using			
Quoted Prices in Active Markets for Identical Instruments	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance	Quoted Prices in Active Markets for Identical Instruments	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance



Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

	(Level 1)			(Level 1)					
Bond funds	\$ 9,384	\$ 0	\$ 0	\$ 9,384	\$ 27,028	\$ 0	\$ 0	\$ 27,028	
Corporate convertible notes	0	0	0	0	0	0	900	900	
<b>Total</b>	<b>\$ 9,384</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 9,384</b>	<b>\$ 27,028</b>	<b>\$ 0</b>	<b>\$ 900</b>	<b>\$ 27,928</b>	

**Table of Contents**

The following table presents changes in Level 3 investments measured on a recurring basis for the six-month periods ended June 30, 2013 and 2012:

	<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2012</b>
Beginning balance	\$ 900	\$ 10,985
Purchases	0	450
Redemption	(900)	(8,956)
Realized gain	0	(2,027)
- Included in other income	0	(40)
- Included in other comprehensive income	0	(1,987)
Exchange difference	0	(2)
Ending balance	\$ 0	\$ 450

**Measured on non-recurring basis**

The Company's financial assets and liabilities measured at fair value on a non-recurring basis include acquired assets and liabilities at initial recognition based on Level 3 inputs in connection with business acquisitions.

The Company measured the fair value of the purchased intangible using the cost, income approach-excess earnings or with & without valuation methods. These purchased intangible assets are considered Level 3 assets because the Company used unobservable inputs, such as forecasted financial performance of the acquired business and discount rates, to determine the fair value of these purchased assets.

**18. EARNINGS PER SHARE**

The following is a reconciliation of the numerators and denominators of the basic and diluted net income per share computations:

	<b>Three Months Ended</b>		<b>Six Months Ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Amounts attributable to AsiaInfo-Linkage, Inc. common stockholders (numerator)				
(Loss) income from continuing operations, net of taxes	\$ (281,499)	\$ 6,226	\$ (268,551)	\$ 12,595
(Loss) income from discontinued operations, net of taxes	0	(1)	1,153	(8)
Net (loss) income	\$ (281,499)	\$ 6,225	\$ (267,398)	\$ 12,587
Shares (denominator):				
Weighted average common stock outstanding				
Basic	72,819,969	72,508,556	72,781,310	72,491,005
Dilutive effect of employee stock options and restricted stock units	0	255,323	0	253,711
Diluted	72,819,969	72,763,879	72,781,310	72,744,716
Earnings per share				
Net (loss) income from continuing operations attributable to AsiaInfo-Linkage, Inc. common				

Edgar Filing: ASIAINFO-LINKAGE, INC - Form 10-Q

stockholders					
Basic	\$	(3.87)	\$	0.09	\$ (3.69) \$ 0.17
Diluted	\$	(3.87)	\$	0.09	\$ (3.69) \$ 0.17
Net (loss) income from discontinued operations attributable to AsiaInfo-Linkage, Inc. common stockholders					
Basic	\$	0.00	\$	0.00	\$ 0.02 \$ 0.00
Diluted	\$	0.00	\$	0.00	\$ 0.02 \$ 0.00
Net (loss) income attributable to AsiaInfo-Linkage, Inc. common stockholders					
Basic	\$	(3.87)	\$	0.09	\$ (3.67) \$ 0.17
Diluted	\$	(3.87)	\$	0.09	\$ (3.67) \$ 0.17

**Table of Contents**

The dilutive effects of the stock options and restricted stock units are calculated using the treasury stock method. Under the treasury stock method, the proceeds from the assumed conversion of stock options and restricted stock units which include the benefit of the compensation costs attributable to future services and not yet recognized, are used to repurchase outstanding shares of common stock using a quarterly average market price.

The Company had 6,317,155 and 6,353,466 stock options outstanding for the three months and six months ended June 30, 2012, respectively, which could potentially dilute earnings per share ( EPS ) in the future, but were excluded from the computation of diluted EPS as their exercise prices were above the average market values during that period. The Company also excluded 85,600 and 90,984 restricted stock units from the computation of diluted EPS for the three months and six months ended June 30, 2012, respectively.

In addition, the Company excluded all stock options and restricted stock units for the three months and six months period ended June 30, 2013, respectively, in the computation of diluted EPS for the three months and six month ended June 30, 2013 as their inclusion would result in a reduction in loss per share.

**19. CHANGES IN ACCUMULATED OTHER COMPREHENSIVE INCOME**

The following table presents the changes in each component of accumulated other comprehensive income (loss), net of tax, for the three months and six months ended June 30, 2013 and 2012, respectively:

	<b>Three Months Ended June 30, 2013</b>		
	<b>Unrealized gain (loss)</b>		<b>Total</b>
	<b>on</b>	<b>Foreign currency</b>	
	<b>available-for-sale</b>	<b>items</b>	
	<b>securities</b>		
Beginning balance	\$ 77	\$ 46,608	\$ 46,685
Other comprehensive income before reclassifications	251	6,656	6,907
Amounts reclassified out of accumulated other comprehensive income	(939)	0	(939)
Net current-period other comprehensive (loss) income	(688)	6,656	5,968
Ending balance	\$ (611)	\$ 53,264	\$ 52,653

**Table of Contents**

<b>Three Months Ended June 30, 2012</b>			
	<b>Unrealized gain (loss)</b>		<b>Total</b>
	<b>on</b>	<b>Foreign currency</b>	
	<b>available-for-sale</b>	<b>items</b>	
	<b>securities</b>		
Beginning balance	\$ 782	\$ 45,458	\$ 46,240
Other comprehensive income before reclassifications	474	(1,922)	(1,448)
Amounts reclassified out of accumulated other comprehensive income	(934)	0	(934)
Net current-period other comprehensive loss	(460)	(1,922)	(2,382)
Ending balance	\$ 322	\$ 43,536	\$ 43,858

<b>Six Months Ended June 30, 2013</b>			
	<b>Unrealized gain (loss)</b>		<b>Total</b>
	<b>on</b>	<b>Foreign currency</b>	
	<b>available-for-sale</b>	<b>items</b>	
	<b>securities</b>		
Beginning balance	\$ (405)	\$ 45,555	\$ 45,150
Other comprehensive income before reclassifications	774	7,709	8,483
Amounts reclassified out of accumulated other comprehensive income	(980)	0	(980)
Net current-period other comprehensive (loss) income	(206)	7,709	7,503
Ending balance	\$ (611)	\$ 53,264	\$ 52,653

<b>Six Months Ended June 30, 2012</b>			
	<b>Unrealized gain (loss)</b>		<b>Total</b>
	<b>on</b>	<b>Foreign currency</b>	
	<b>available-for-sale</b>	<b>items</b>	
	<b>securities</b>		
Beginning balance	\$ 2,211	\$ 44,913	\$ 47,124
Other comprehensive income before reclassifications	768	(1,377)	(609)
Amounts reclassified out of accumulated other comprehensive income	(2,657)	0	(2,657)
Net current-period other comprehensive loss	(1,889)	(1,377)	(3,266)
Ending balance	\$ 322	\$ 43,536	\$ 43,858

**Table of Contents**

The following table presents the reclassification out of accumulated other comprehensive income (loss) for the three months and six months ended June 30, 2013 and 2012 respectively:

	Three Months Ended June 30					
	Before Tax		Tax Effect		Net of Tax	
	2013	2012	2013	2012	2013	2012
Net unrealized loss on investment securities:						
Net unrealized gain arising during the period	292	607	41	133	251	474
Less: reclassification adjustment for gain realized and recorded as gain from sales of short-term investments	1,105	1,245	166	311	939	934
Net unrealized loss on investment securities	\$ (813)	\$ (638)	\$ (125)	\$ (178)	\$ (688)	\$ (460)

	Six Months Ended June 30					
	Before Tax		Tax Effect		Net of Tax	
	2013	2012	2013	2012	2013	2012
Net unrealized loss on investment securities:						
Net unrealized gain arising during the period	927	1,001	153	233	774	768
Less: reclassification adjustment for gain realized and recorded as gain from sales of short-term investments	1,153	3,272	173	615	980	2,657
Net unrealized loss on investment securities	\$ (226)	\$ (2,271)	\$ (20)	\$ (382)	\$ (206)	\$ (1,889)

**20. GOVERNMENT SUBSIDIES**

Government subsidies include amounts granted by government authorities to encourage research and development for high-technology companies. Subsidies are recognized in the Company's financial statements once the approvals are obtained from the relevant government authorities and the Company has the right to receive the subsidies.

If the subsidy is granted in connection with a specific project, it would be recorded as a reduction to cost of revenues. Otherwise, the subsidy is recorded as other operating income. For the three-month periods ended June 30, 2013 and 2012, the Company recognized government subsidies as a reduction to costs of revenues of \$1,241 and \$0, respectively, and government subsidies in other operating income of \$273 and \$0, respectively. For the six-month periods ended June 30, 2013 and 2012, the Company recognized government subsidies as a reduction of costs of revenues of \$1,241 and \$1,891, respectively, and government subsidies in other operating income of \$273 and \$0, respectively.

---

**Table of Contents**

**21. SEGMENT INFORMATION**

The Company's operations are currently organized into five business units by three telecommunication carriers in China, multiple Cable Television providers in China, and telecommunication carriers internationally. In accordance with FASB guidance, each of these five business units represents an operating segment, of which discrete financial information is available and is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. The five operating segments are aggregated into one reportable segment because they meet the aggregation criteria of FASB and have the same economic characteristics.

The Company's chief operating decision maker is the Company's Business Committee, comprising the Company's Chief Executive Officer, Chief Financial Officer, Chief Technology Officer and senior management team.

The Company primarily operates in the PRC and substantially all of the Company's long-lived assets are located in the PRC.

**22. COMMITMENTS AND CONTINGENCIES**

***Commitments***

In May 2011, the Company entered into a land use right transfer agreement with the Beijing Municipal Bureau of Land and Resources, under which the Company acquired land use right for a 50-year term. Pursuant to the agreement, the Company has committed a minimum of \$17,902 as of June 30, 2013 for capital expenditures to the building construction project, to commence construction by April 30, 2012, and to complete construction by April 30, 2014.

In November 2011, the Company entered into a software purchase agreement with IBM, through which the Company is committed to purchase software from IBM and is expected to be paid from 2012 to 2014. As of June 30, 2013, the Company committed to purchase software from IBM amounting to \$3,236. The committed purchase amounts are \$1,618 and \$1,618 for the next two years respectively.

***Contingencies Litigations***

In October 2012, a putative stockholder of the Company filed a civil action, derivatively on behalf of the Company, against the members of the board of directors and certain officers. The Company was also named as a nominal defendant. The action was filed in the United States District Court for the District of Delaware. The plaintiff asserted claims for breach of fiduciary duty against all defendants, corporate waste against the director defendants, and unjust enrichment against the officer defendants in connection with grants of stock options allegedly made in an amount that purportedly violates certain limitations set forth in the Company's 2011 Stock Incentive Plan. The plaintiff seeks rescission of the option grants in question, an award of unspecified damages to the Company, certain other equitable and injunctive relief, and an award of plaintiff's costs and disbursements, including legal fees. In January 2013, the Company and the individual defendants filed a motion to dismiss the action. On March 18, 2013, plaintiffs filed an opposition to defendants' motion, and on April 17, 2013, defendants filed a reply. On July 18, 2013, defendants filed a notice of subsequent authority. The motion to dismiss remains pending.

Upon the unanimous recommendation of the Special Committee of its Board of Directors and the approval of its Board of Directors, on May 12, 2013, the Company entered into an Agreement and Plan of Merger (the "Merger Agreement"), with Skipper Limited ("Parent") and Skipper Acquisition Corporation ("Merger Sub"), which are owned indirectly by CITIC Capital Partners, the private equity arm of CITIC Capital Holdings Ltd. Pursuant to the terms and subject to the conditions of the Merger Agreement, Merger Sub would merge (the "Merger") with and into the Company, with the Company continuing as the surviving corporation and a wholly owned subsidiary of Parent, and each share of outstanding Company common stock would convert automatically into the right to receive US\$12.00 in cash without interest, except for dissenting shares, shares of treasury stock, and shares held members of the buyer group that will own all of Parent following the Merger.

## **Table of Contents**

Since the announcement that the Company entered into the Merger Agreement, certain alleged Company stockholders have filed three putative class actions against the Company, the members of its Board of Directors and Merger Sub in the Delaware Court of Chancery, under the captions *Guanghai Cai v. AsiaInfo-Linkage, Inc., et al.*, C.A. No. 8583-VCP, *Dawan Liu v. AsiaInfo-Linkage, Inc., et al.*, C.A. No. 8634-VCP, and *Loren Lowry v. AsiaInfo-Linkage, Inc., et al.*, C.A. No. 8695-VCP. Plaintiffs allege that the Company's Board of Directors breached their fiduciary duties to the Company's stockholders by favoring Parent over other potential purchasers, favoring their own interests over the interests of the Company's stockholders, failing to take appropriate steps to maximize the value of the Company to its stockholders, agreeing to preclusive deal protection devices and otherwise agreeing to sell the Company for an unfairly low price. Plaintiffs further allege that the Company and Merger Sub aided and abetted those alleged breaches of fiduciary duty. Plaintiffs have requested an injunction, rescission of the Merger to the extent consummated, money damages if the Merger is consummated, certain other equitable relief, and an award of plaintiffs' costs, including legal fees. Plaintiffs in the *Liu* action have also requested a declaration that the Merger is unfair, unjust and inequitable.

While the Company cannot guarantee the outcome of these proceedings, the Company believes that the final results will not have a material effect on its consolidated financial condition, results or operations, or cash flows.

### ***Contingencies Letters of Credit***

As of June 30, 2013, the Company had outstanding standby letters of credit in the amount of \$23,254. They were used for performance guarantees amounting to \$21,091 with respect to the Company's performance on certain customer projects, and guarantees amounting to \$2,163 with respect to future payments for building construction.

### **23. NONCONTROLLING INTEREST**

(a) On September 25, 2008, the Company established a new subsidiary, Shanghai Xinjia Science & Technology Co., Ltd ( AISH ) in Shanghai, with a total capital contribution of \$732. The Company and Ms. Yao Yuan, the other shareholder of AISH, hold 90% and 10% of AISH's share capital, respectively. AISH mainly provides software and services to telecommunication carriers in Shanghai. The 10% of AISH's share capital held by Ms. Yao Yuan was recorded as noncontrolling interest.

(b) In October 2009, the Company acquired 60% of the share capital of SmartCall Holding Limited ( Smartcall ) and the remaining 40% of the share capital was recorded as noncontrolling interest. In May 2013, the Company disposed of its interest in Smartcall together with Smartcall's interest in a VIE named ZXJ.

(c) In September 2011, the Company's VIE Beijing Star VATS acquired 60% of the share capital of Chengdu Yalian Zhixing Technology Ltd ( Yalian Zhixing ). The remaining 40% of the share capital was recorded as noncontrolling interest. In May 2013, the Company disposed of its interest in Beijing Star VATS, together with its 60% share capital of Yalian Zhixing.

### **24. REDEEMABLE NONCONTROLLING INTEREST**

(a) In October 2009, the Company formed AsiaInfo International Pte Ltd ( AIP ) with Alpha Growth International Pte Ltd, a company incorporated under the laws of Singapore ( AGI ), in Singapore. AIP has total issued and paid-up share capital of \$4,000. The Company contributed \$2,800 to AIP in cash, which represents 70% of AIP's share capital. AGI contributed \$1,200 to AIP in cash, which represents 30% of AIP's share capital. AIP serves as an exclusive agent to market and distribute the Company's telecommunications software and service solutions in certain regions in Southeast Asia until December 2014 or such other date as the Company and AGI may mutually agree. The Company has consolidated AIP since its incorporation.

Pursuant to the agreement with AGI, the Company granted a put option to AGI to sell, while the Company received a call option from AGI to purchase, the 30% equity interest held by AGI. The options are exercisable within a 30 day-period from the date of issuing the audit report of AIP's 2013 financial statements. The exercise prices for the call and the put options of the 30% equity interest held by AGI are the same and are determined by a formula based on the performance of AIP for years 2012 and 2013.



**Table of Contents**

(b) In May 2010, the Company, through a subsidiary of the Company, acquired an 80% equity interest in Hangzhou Zhongbo for an aggregate purchase price of \$7,068 in cash. Hangzhou Zhongbo provides IT solutions to broadcasting operators in China.

Pursuant to the agreement with the other shareholder of Hangzhou Zhongbo, the Company granted a put option to such shareholder of Hangzhou Zhongbo to sell, while the Company received a call option from such shareholder of Hangzhou Zhongbo to purchase, the 20% equity interest held by such shareholder in Hangzhou Zhongbo. The options were exercisable after December 31, 2011. The exercise prices for the call and the put options of the 20% equity interest held in Hangzhou Zhongbo were the same and were determined by a formula based on the performance of Hangzhou Zhongbo for years 2010 and 2011.

In June 2012, the Company exercised the call option and purchased the remaining 20% equity interest in Hangzhou Zhongbo for a consideration of \$1,034. As a result, the Company holds 100% equity interest in Hangzhou Zhongbo.

These noncontrolling interests were recorded outside of the permanent equity on the consolidated balance sheets initially at the fair value of the noncontrolling interests as of the date of incorporation or the date of acquisition of these subsidiaries. Subsequently, each noncontrolling interest was carried at the higher of (1) the initial carrying amount, increased or decreased for the noncontrolling interest's share of net income or loss or (2) the accreted amount to the expected redemption value. The change of the carrying amounts of the redeemable noncontrolling interest is recognized as net income attributable to noncontrolling interest in the consolidated statements of operations. For the six months ended June 30, 2013, the amount charged to net loss attributable to noncontrolling interests was \$1,397, which represents the noncontrolling interests' share of net loss of these subsidiaries.

	<b>Redeemable Noncontrolling Interest</b>
<b>Balance at January 1, 2013</b>	\$ (3,488)
Net loss	(854)
Adjustment to redemption value	0
<b>Balance at March 31, 2013</b>	\$ (4,342)
Net loss	(543)
Adjustment to redemption value	0
<b>Balance at June 30, 2013</b>	\$ (4,885)

---

**Table of Contents**

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Except for historical information, the statements contained in this quarterly report on Form 10-Q are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. The Private Securities Litigation Reform Act of 1995, or the Reform Act, contains certain safe harbors regarding forward-looking statements. Certain of the forward-looking statements include management's expectations, intentions and beliefs with respect to our growth, our operating results, the nature of the industry in which we are engaged, our business strategies and plans for future operations, our needs for capital expenditures, capital resources and liquidity, and similar expressions concerning matters that are not historical facts. Such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in the statements. All forward-looking statements included in this report are based on information available to us on the date hereof, and we assume no obligation to update any such forward-looking statements. These cautionary statements are being made pursuant to the provisions of the Reform Act with the intention of obtaining the benefits of the safe harbor provisions of the Reform Act. The factors that could cause actual results to differ materially include, but are not limited to, the factors discussed under the heading "Risk Factors" in our Form 10-K for the year ended December 31, 2012 and in the reports we file with the U.S. Securities and Exchange Commission, or the SEC, from time to time.

In this report, the Company, we, us and our refer to AsiaInfo-Linkage, Inc. and its subsidiaries, Linkage refers to Linkage Technologies International Holdings Limited, and AsiaInfo refers to the Company prior to its combination with Linkage.

**Overview**

We are the leading provider of high-quality telecommunications software solutions and information technology, or IT, products and services in China. Our solutions, products and services include business support systems, or BSS, containing billing and customer relationship management, or CRM, and other software and services. Our software and services enable our customers to build, maintain, operate, manage and improve their communications infrastructure. Our largest customers are the major telecommunications carriers in China and their provincial subsidiaries, including China Mobile Communications Corporation, or China Mobile, China United Telecommunications Corporation, or China Unicom, and China Telecommunications Corporation, or China Telecom.

We are also the leading provider in China's cable television BSS market, providing billing and CRM software and services. We won several important contracts to provide modernized BSS for consolidated provincial-level cable operators in most of the key provinces in China, such as Jiangsu Cable TV and Zhejiang Cable TV. We believe the successful implementation of these projects has brought additional value to our customers and positions us well for future cable industry consolidation among multiple regional operators, which we expect to accelerate in the coming years.

We are also expanding our footprint in the international telecommunications software and services market by leveraging the valuable experience gained from our Chinese telecommunications carriers. In 2011, we won new contracts from customers in Southeast Asia, including Malaysia, Nepal and others, after an detailed selection process against other industry leading vendors, which is a significant achievement given the long selling cycle of business support software. In June 2012, we opened our first European based sales office in Cambridge, United Kingdom as part of our ongoing initiative to expand operations across Europe, Middle East and Africa (EMEA) markets. In 2013, we plan to continue to expand our international business through both our Southeast Asia offices and our European office by signing new telecommunication carrier customers and by providing additional software and services to current customers.

We commenced our operations in the United States, or the U.S., in 1993 and moved our major operations from the U.S. to China in 1995. We began generating significant network solutions revenues in 1996 and significant software revenues in 1998. We conduct the bulk of our business through our operating subsidiaries, most of which are Chinese companies. On July 1, 2010, we completed the combination with Linkage and, in connection with the closing, changed our corporate name to AsiaInfo-Linkage, Inc.

**Table of Contents**

We have derived, and believe that we will continue to derive, a significant portion of our revenues from a limited number of large telecommunications customers, such as China Mobile, China Unicom and China Telecom and their respective provincial subsidiaries. The following table shows our revenues and percentage of total revenues derived from those three customers (and their respective provincial subsidiaries) for the three months ended June 30, 2013 and 2012.

	Three Months Ended June 30,			
	2013		2012	
	Revenues (in thousands)	Percentage of Total Revenues	Revenues (in thousands)	Percentage of Total Revenues
China Mobile	\$ 65,710	47%	\$ 67,103	53%
China Telecom	26,183	19%	22,266	18%
China Unicom	42,376	30%	33,059	26%
Total	\$ 134,269	96%	\$ 122,428	97%

As a result of our reliance on our key customers in the telecommunications industry, our operating results are influenced by governmental spending policies in that sector. Historically, there have been a number of state-mandated restructurings in China's telecommunications sector. Some of these restructurings have led to cancellation or delays in telecommunications-related capital expenditures that have negatively impacted our operating results in certain periods. Other restructurings have caused our revenues to increase as carriers have increased spending on software and IT infrastructure designed to increase their competitiveness. Any future restructurings affecting our major telecommunications customers could have an adverse impact on our business.

For financial reporting purposes, we present our revenues as follows:

Software products and solutions;

Services; and

Third-party hardware.

**Recent Developments**

On January 20, 2012, we announced the receipt of a non-binding proposal letter from Power Joy (Cayman) Limited, or Power Joy, a wholly owned subsidiary of CITIC Capital China Partners II, L.P., or CITIC, pursuant to which Power Joy proposed to acquire all of our outstanding shares of common stock in cash at a price that represents a premium over the stock price. A special committee of the board of directors, or the Special Committee, was formed to consider the proposal and any potential alternative transactions. The Special Committee retained Shearman & Sterling LLP as its legal counsel and Goldman Sachs (Asia) L.L.C. as its financial advisor to assist it in consideration of such matters. On March 26, 2012, we announced that the Special Committee would solicit interest from, and engage in discussions with, other potential qualified interested parties regarding a potential transaction involving us, and to evaluate any proposals it receives. Upon the unanimous recommendation of the Special Committee and the approval of our board of directors, on May 12, 2013, we entered into an Agreement and Plan of Merger, or the Merger Agreement, with Skipper Limited, or Parent, and Skipper Acquisition Corporation, or Merger Sub, which are owned indirectly by CITIC. Pursuant to the terms and subject to the conditions of the Merger Agreement, Merger Sub would merge with and into us, we would continue as the surviving corporation and a wholly owned subsidiary of Parent, and each share of our outstanding common stock would convert automatically into the right to receive \$12.00 in cash without interest, except for dissenting shares, shares of treasury stock, and shares held members of the buyer group that will own all of Parent following the transaction. We refer to this transaction as the Merger. If the Merger closes pursuant to the Merger Agreement, we would cease to be listed on the NASDAQ Stock Market or a public reporting company in the U.S. The Merger Agreement is subject to closing conditions, including stockholder approval, and there can be no assurance that the Merger or any other transaction will be approved or consummated.

---

## **Table of Contents**

On January 29, 2013, we announced the successful implementation of our Veris Billing system for the Code Division Multiple Access, or CDMA, network of Nepal Doorsanchar Company Limited, or Nepal Telecom, the largest telecommunications operator in Nepal. This first phase of what is a comprehensive software upgrade for Nepal Telecom was completed within four months from the start of the project and provided fully convergent billing and real-time online charging for pre-paid and postpaid subscribers on the carrier's CDMA network.

On February 5, 2013, we announced that our advanced Veris suite of Business Support Systems and solutions are available in the markets of Europe, the Middle East and Africa. Our comprehensive Veris portfolio, which is already deployed in Asia, includes the core solutions of Veris Billing, Veris CRM and Veris BI. These products, and some of their industry-leading individual components, can be deployed as standalone modules or as complete, pre-integrated solutions.

On April 8, 2013, we announced that two of our subsidiaries in China, AsiaInfo-Linkage Technologies (China), Inc., or AIBJ and Linkage-AsiaInfo Technologies (Nanjing), Inc., or Linkage Nanjing had been formally granted Key Software Enterprise, or KSE, status under China's Enterprise Income Tax Law. As a result, AIBJ and Linkage Nanjing became eligible for a preferential corporate income tax rate of 10% for the years 2011 and 2012. KSE status is currently granted every two years after formal government review. We applied for KSE status on behalf of AIBJ and Linkage Nanjing in October of 2012, when the relevant PRC tax authorities released the application requirements for the years 2011 and 2012. As there had been no guarantee that KSE status would ultimately be granted, we had previously used a rate of 15% in computing the 2011 and 2012 taxes for both AIBJ and Linkage Nanjing.

On May 24, 2013, we announced the sale of our interests in two contractually controlled entities, namely, Beijing Zhongxinjia Sci-Tech Development Co., Ltd. and Beijing Star VATS Technologies Co., Inc.

## **Revenues**

We recognize revenue pursuant to the requirements of the Financial Accounting Standards Board, or the FASB, Accounting Standards Codification, or the ASC, when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectability is probable, and other applicable revenue recognition guidance and interpretations.

Our revenue is derived from three primary sources: (i) software licenses and related services, including implementation, customization and integration, post-contract customer support, or PCS, training and consulting; (ii) professional services for systems design, planning, consulting, and system integration; and (iii) the procurement of hardware on behalf of customers.

Our multiple-element arrangements relate to our software licenses and related services, including implementation, customization and integration, PCS, training, consulting and third-party hardware procurement.

**Software products and solutions revenue.** Revenues of software licenses and related services, including implementation, customization and integration, PCS, training and consulting, are recognized using the percentage of completion method over the service period based on the relationship of costs already incurred to the total estimated costs to be incurred because such customer orders require significant production, modifications, or customization of the software. For China projects, we consider total project costs (labor costs and other related costs) in calculating the percentage of completion and recognize cost of sales on an actual basis with no deferral of project costs, including pre-contract costs. Software arrangements with significant production, modifications, or customization are sold with bundled third-party hardware and PCS services. Because PCS services have never been sold separately in these arrangements, they do not have stand-alone fair value or vendor-specific objective evidence, or VSOE, of fair value. The percentage of completion method of revenue recognition is therefore applied to the period from the start of the significant production, modifications, or customization through the last element delivered, which is typically the end of the bundled PCS services period. Revisions in estimated contract costs are made in the period in which the circumstances requiring the revision become known. Provisions, if any, are made currently for anticipated losses on uncompleted contracts. For certain projects outside of China, we defer revenue and cost until the revenue recognition criteria have been met.

**Table of Contents**

**Service revenue.** Revenues of professional services for systems design, planning, consulting, and system integration are recognized when the services are performed.

In addition, we generate service revenues by acting as a sales agent for International Business Machines Corporation, or IBM, or its distributors, and a few other hardware vendors, for certain products sold to our customers, which we refer to as our IBM-Type Arrangements. The service fee under the IBM-Type Arrangements is determined as a percentage of the gross contract amount. We have evaluated the criteria outlined in guidance issued by the Financial Accounting Standards Board, or the FASB, regarding reporting revenue gross as principal versus net as an agent, in determining whether to record as revenues the gross amount billed to our customers and related costs or the net amount earned after deducting hardware costs paid to the vendor, even though we bear inventory risks after the vendor ships the products to us and we bill gross amounts to our customers. We record the net amount earned after deducting hardware costs as agency service revenue because (1) the vendor is the primary obligor in these transactions, (2) we have no latitude in establishing the prices, (3) we are not involved in the determination of the product specifications, (4) we do not bear credit risk because we are contractually obligated to pay the vendor only when the customers pay us, and (5) we do not have the right to select suppliers.

**Third-party hardware revenue.** Revenues of the procurement of hardware on behalf of customers, if not bundled with other arrangements, are recognized when shipped and customer acceptance obtained, if all other revenue recognition criteria are met. Costs associated with revenues are recognized when incurred. If bundled with other arrangements, we generally bifurcate the third-party hardware from the development services and recognize the hardware revenue upon customer acceptance using estimated prices based on cost plus a margin, which we believe to be the fair value of the selling price.

**Net revenue.** Although we report our revenue on a gross basis, inclusive of hardware acquisition costs, we manage our business internally based on revenues net of hardware costs, or net revenues, a non-GAAP measure. We believe this approach is consistent with our strategy of providing our customers with high value IT professional services and, where efficient, outsourcing lower-end services such as hardware acquisition and installation. The following table shows our revenue breakdown on this basis and reconciles our net revenues to total revenues:

	<b>Three Months Ended June 30,</b>	
	<b>2013</b>	<b>2012</b>
Revenues net of hardware costs:		
Software products and solutions revenue	\$ 127,554	\$ 116,772
Service revenue	8,909	7,553
Third-party hardware revenue net of hardware costs	188	98
<b>Total revenues net of hardware costs</b>	<b>136,651</b>	<b>124,423</b>
Total hardware costs	3,557	1,848
<b>Total revenues</b>	<b>\$ 140,208</b>	<b>\$ 126,271</b>

	<b>Six Months Ended June 30,</b>	
	<b>2013</b>	<b>2012</b>
Revenues net of hardware costs:		
Software products and solutions revenue	\$ 257,027	\$ 230,834
Service revenue	14,775	14,507
Third-party hardware revenue net of hardware costs	572	232
<b>Total revenues net of hardware costs</b>	<b>272,374</b>	<b>245,573</b>
Total hardware costs	10,859	4,395
<b>Total revenues</b>	<b>\$ 283,233</b>	<b>\$ 249,968</b>



## **Table of Contents**

We believe total revenues net of hardware costs more accurately reflects our core business, which is the provision of software solutions and services, and provides transparency to our investors. We believe this measure provides transparency to our investors because it is the measure used by our management to evaluate the competitiveness and performance of our business. In addition, third-party hardware revenue tends to fluctuate from period to period depending on the requirements of our customers. As a result, a presentation that excludes hardware costs allows investors to better evaluate the performance of our core business.

### **Cost of Revenues**

**Software products and solutions costs.** Software products and solutions costs consist primarily of three components:

packaging and written manual expenses for our proprietary software products and solutions;

compensation and travel expenses for the professionals involved in modifying, customizing or installing our software products and solutions and in providing consultation, training and support services; and

software license fees paid to third-party software providers for the right to sublicense their products to our customers as part of our solutions offerings.

The costs associated with designing and modifying our proprietary software are classified as research and development, or R&D, expenses as incurred.

The costs incurred for the implementation phases of projects outside of China, which provide multiple services and products (software, hardware, implementation, maintenance and managed services), are deferred and capitalized as inventories during the system implementation phase, and transferred to cost of sales upon revenue recognition.

**Service costs.** Service costs consist primarily of compensation and travel expenses for the professionals involved in designing and implementing IT services, management consulting and network solutions projects.

**Third-party hardware costs.** We generally recognize hardware costs in full upon delivery of the hardware to our customers. In order to minimize our working capital requirements, we generally obtain from our hardware vendors payment terms that are timed to permit us to receive payment from our customers for the hardware before our payments to hardware vendors are due. However, in large projects we sometimes obtain less favorable payment terms from our customers, thereby increasing our working capital requirements.

Amortization of intangible assets, depreciation of properties and equipment, and rental expenses are also included in cost of revenue.

### **Operating Expenses**

Operating expenses consist of sales and marketing expenses, general and administrative expenses and R&D expenses. Amortization of acquired intangible asset expenses consistently comprise a significant portion of our total operating expenses.

Sales and marketing expenses include compensation expenses for employees in our sales and marketing departments, third-party advertising expenses, marketing events, sales commissions and sales consulting fees, as well as the depreciation and amortization expenses allocated to our sales and marketing departments.

R&D expenses relate to the development of new software and the modification of existing software. We expense such costs as they are incurred.

## **Table of Contents**

General and administrative expenses include compensation expenses for employees in our general and administrative departments, third-party professional services fees, and the depreciation expenses allocated to our general and administrative departments.

Government subsidies represent rewards from government for the high-tech software innovation.

## **Taxes**

Except for certain hardware procurement and resale transactions, we conduct substantially all of our business through our Chinese subsidiaries and VIEs. To a smaller degree, our operations in Southeast Asia are conducted through our joint venture in Singapore and its subsidiaries. Prior to the enactment of China's current Enterprise Income Tax Law, or the EIT Law, which became effective on January 1, 2008, foreign-invested enterprises, or FIEs, were generally subject to a 30% state enterprise income tax plus a 3% local income tax. However, most of our operating subsidiaries in China, as FIEs, were entitled to tax holidays or certain preferential tax treatments, which thus reduced their effective rate of income tax to 15% or lower in some cases. Since the EIT Law became effective, all resident enterprises are subject to a flat 25% income tax rate, unless they are otherwise eligible for certain preferential tax treatments under the new rules.

Pursuant to implementation and transition rules related to the EIT Law, certain of our subsidiaries in China may enjoy a 15% preferential tax rate if they are qualified as High-and-New Technology Enterprises, or HNTE, while other of our subsidiaries and VIEs became subject to the 25% income tax rate. HNTE status is valid for three years. At the conclusion of the three-year period, the qualifying enterprise has the option to renew its HNTE status for an additional three years through a simplified application process if such enterprise's business operations continue to qualify for HNTE status. After the first six years, the enterprise would be subject to a new application process in order to renew its HNTE status. We received HNTE certification for AIBJ, AsiaInfo-Linkage Technologies (Chengdu), Inc., or AICD, and Linkage Nanjing at the end of 2011 and the beginning of 2012, respectively, which allows those companies to compute tax at a reduced 15% tax rate from January 1, 2011 until December 31, 2013. As such, we computed tax at a reduced 15% tax rate for AIBJ, AICD and Linkage Nanjing for the estimated annual effective tax rate of 2013.

AIBJ and Linkage Nanjing were approved as Key Software Enterprises, or KSEs, and were eligible for a further reduction in their tax rate to 10% for 2011 and 2012. AIBJ and Linkage Nanjing will apply for 2013 KSE status once the government authorities in charge release the application requirements. As such, we have computed our current quarterly taxes based on the tax rate of 15% for both AIBJ and Linkage Nanjing.

Sales of hardware procured in China are subject to a 17% value added tax, or VAT. Most of our sales of hardware procured outside of China are made through our U.S. parent company, AsiaInfo-Linkage, Inc., or one of its subsidiaries, Hong Kong AsiaInfo-Linkage Technologies Ltd., and thus are not subject to the VAT. We effectively pass VAT on hardware sales through to our customers and do not include VAT in revenue reported in our financial statements. Companies that develop their own software and register the software with relevant authorities in China are generally entitled to a VAT refund. If the net amount of the VAT payable exceeds 3% of software sales and software-related services, the excess portion of the VAT is refundable immediately. The policy was extended by a new tax circular issued in January 2011. The benefit of the VAT rebate is included in software revenue. Historically, the VAT refund received has not been taxable for income tax purposes as long as the refund is used for R&D activities. However, according to a tax circular issued by the PRC State Administration of Taxation in 2009, although the VAT refund would remain non-taxable, all the expenses associated with the refund are not tax deductible for income tax purposes. This circular also stipulates that any VAT refund not spent within the five-year period following its receipt must be added back to taxable income in the sixth year. In accordance with instructions from certain local tax jurisdictions, we report VAT refund as taxable income in calculating our income tax provision for certain years.



---

## **Table of Contents**

Our PRC subsidiaries and VIEs are subject to business tax at the rate of 3% or 5%, respectively, on certain types of service revenues, which are presented in our statements of operations net of business tax incurred.

Effective from December 1, 2010, our PRC subsidiaries and VIEs are also subject to Urban Maintenance and Construction Tax as well as Education Fee Surcharge at the rate of 7% and 3% of VAT and business taxes paid, respectively.

In January 2011, the State Council issued a circular providing an exemption from business tax for eligible software companies on software development and testing, system integration, consulting and maintenance services. The circular also retains various policies granted by previous circulars, including the VAT rebate on sales of software. The implementation guidance of this new circular has not been issued as of the date of this report, although implementation guidance for value-added tax rebates on sales of software was issued in October 2011.

In July 2012, the Ministry of Finance and the State Administration of Taxation jointly issued a circular regarding the pilot collection of VAT in lieu of business tax in certain areas and industries in the PRC. Such VAT pilot program is to be phased in Beijing, Jiangsu, Anhui, Fujian, Guangdong, Tianjin, Zhejiang, and Hubei between September and December 2012. Starting from September 1, 2012, certain subsidiaries and VIEs became subject to VAT at the rates of 6% or 3%, on certain service revenues which were previously subject to business tax.

We are also subject to U.S. income taxes on revenues generated in the U.S., including revenues from our limited hardware procurement activities through our U.S. parent company, AsiaInfo-Linkage, Inc., and interest income earned in the U.S.

### **Foreign Exchange**

A majority of our revenues and expenses relating to hardware sales and the software and service components of our business are denominated in RMB. The value of our shares will be affected by the foreign exchange rate between U.S. dollars and RMB because the value of our business is effectively denominated in RMB, while our shares are traded in U.S. dollars. In addition, as we pursue our global strategy, we need to settle transactions in various currencies of Southeast Asian countries, expect to continue to do so in future, and expect that such activities may create similar foreign exchange risk associated with the currencies of these jurisdictions. Depreciation of the value of the U.S. dollar will also reduce the value of the cash we hold in U.S. dollars, which we may use for purposes of future acquisitions or other business expansion. We actively monitor our exposure to these risks and adjust our cash position in the RMB and the U.S. dollar when we believe such adjustments will reduce our foreign exchange risks and otherwise appropriate. We did not engage in any significant foreign exchange transactions during the six-month period ended June 30, 2013.

As of June 30, 2013, approximately 89.2%, or \$264.1 million, of our cash, cash equivalents and restricted cash were RMB-denominated and approximately 10.5%, or \$31.0 million, were U.S. dollar-denominated. Pursuant to the rate of exchange quoted by People's Bank of China as of June 30, 2013, the exchange rate between the U.S. dollar and the RMB was US\$1.00 = RMB6.1787, compared to the rate of US\$1.00 = RMB6.3249 as of June 30, 2012.

### **Critical Accounting Policies**

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States, or US GAAP. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amount of revenues and expenses during the reporting period. On an ongoing basis, we evaluate our estimates and judgments, including those related to revenues and cost of revenues under customer contracts, bad debts, inventories, short-term investments, long-term investments, income taxes, goodwill and other intangible assets, stock options, and litigation. We base our estimates and judgments on historical experience and on various other factors that we believe are reasonable. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies involve the more significant judgments and estimates used in the preparation of our consolidated financial statements.

---

**Table of Contents**

**Revenue recognition.** We recognize revenue when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectability is probable, and other applicable revenue recognition guidance and interpretations.

Our revenue is derived from three primary sources: (i) software licenses and related services, including implementation, customization and integration, post-contract customer support, or PCS, training and consulting; (ii) professional services for systems design, planning, consulting, and system integration; and (iii) the procurement of hardware on behalf of customers.

Our multiple-element arrangements relate to our software licenses and related services, including implementation, customization and integration, PCS, training, consulting and third-party hardware procurement.

Revenues of software licenses and related services, including implementation, customization and integration, PCS, training and consulting, are recognized using the percentage of completion method over the service period based on the relationship of costs already incurred to the total estimated costs to be incurred because such customer orders require significant production, modifications, or customization of the software. For China projects, we consider total project costs (labor costs and other related costs) in calculating the percentage of completion and recognize cost of sales on an actual basis with no deferral of project costs, including pre-contract costs. Software arrangements with significant production, modifications, or customization are sold with bundled third-party hardware and PCS services. Because PCS services have never been sold separately in these arrangements, they do not have stand-alone fair value or VSOE of fair value. The percentage of completion method of revenue recognition is therefore applied to the period from the start of the significant production, modifications, or customization through the last element delivered, which is typically the end of the bundled PCS services period. Revisions in estimated contract costs are made in the period in which the circumstances requiring the revision become known. Provisions, if any, are made currently for anticipated losses on uncompleted contracts. For certain projects outside of China, we defer revenue and cost until the revenue recognition criteria have been met.

Revenues of professional services for systems design, planning, consulting, and system integration are recognized when the services are performed.

In addition, we generated service revenues by acting as a sales agent pursuant to the IBM-Type Arrangements. The service fee under our IBM-Type Arrangements is determined as a percentage of the gross contract amount. We have evaluated the criteria outlined in guidance issued by FASB regarding reporting revenue gross as principal versus net as agent, when determining whether we would record as revenues the gross amount billed to our customers and related costs or the net amount earned after deducting hardware costs paid to the vendor, even though we bear inventory risks after the vendor ships the products to us and we bill gross amounts to our customers. We record the net amount earned after deducting hardware costs as agency service revenue because (1) the vendor is the primary obligor in these transactions, (2) we have no latitude in establishing the prices, (3) we are not involved in the determination of the product specifications, (4) we do not bear credit risk because we are contractually obligated to pay the vendor only when the customers pay us, and (5) we do not have the right to select suppliers.

Revenues of the procurement of hardware on behalf of customers, if not bundled with other arrangements, are recognized when shipped and customer acceptance obtained, if all other revenue recognition criteria are met. Costs associated with revenues are recognized when incurred. If bundled with other arrangements, we generally bifurcate the third-party hardware from the development services and recognize the hardware revenue upon customer acceptance using estimated prices based on cost plus a margin, which we believe to be the fair value of the selling price.

Revenue recognized in excess of billings is recorded as unbilled receivables and is included in accounts receivable. Amounts billed but not yet collected are recorded as billed receivables and are included in accounts receivable. All billed and unbilled amounts are expected to be collected within one year. Billings for installation and customization services are rendered based on agreed upon milestones specified in customer contracts. Billings in excess of revenues recognized are recorded as deferred revenue.

## **Table of Contents**

**Income taxes.** Deferred income taxes are provided using the asset and liability method. Under this method, deferred income taxes are recognized for tax credits and net operating losses available for carry-forwards and significant temporary differences. Deferred tax assets and liabilities are classified as current or non-current based upon the classification of the related asset or liability in the financial statements or the expected timing of their reversal if they do not relate to a specific asset or liability.

We record a valuation allowance to reduce our deferred tax assets to the amount that we believe is more likely than not to be realized. In the event we were to determine that we would be able to realize our deferred tax assets in the future in excess of their recorded amount, an adjustment to the deferred tax asset would increase income in the period such determination was made. Likewise, should we determine that we would not be able to realize all or part of our net deferred tax assets in the future, an adjustment to the valuation allowance would be charged to income in the period such change occurred.

The impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than not to be sustained upon audit by the relevant tax authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Interest and penalties on income taxes will be classified as a component of the provisions for income taxes.

The HNTE certificates of AIBJ, AICD and Linkage Nanjing were renewed at the end of 2011 and the beginning of 2012, respectively, which allows those companies to continue to enjoy a 15% preferential tax rate from January 1, 2011 until December 31, 2013.

AIBJ and Linkage Nanjing were KSEs eligible for a 10% tax rate for 2011 and 2012. AIBJ and Linkage Nanjing will apply for 2013 KSE status once the government authorities in charge release the application requirements. As such, we have computed our current quarterly taxes based on the tax rate of 15% for both AIBJ and Linkage Nanjing.

Under the EIT Law, a resident enterprise, which may include an enterprise established outside of the PRC with management located in the PRC, will be subject to PRC income tax. We believe we and our subsidiaries established outside the PRC are not resident enterprises under the EIT law.

**Intangible assets and goodwill.** Intangible assets consist of certain identifiable intangible assets resulting from business acquisitions and primarily comprise customer relationships, trade name, core technologies and existing technology. We amortize these intangible assets over their respective estimated useful lives, which range from 0.5 to 19 years. Intangible assets are reviewed for impairment when events or changes in circumstances indicate that their carrying amounts may not be recoverable based upon the estimated undiscounted cash flows.

The excess of the purchase price over the fair value of net assets acquired is recorded on the consolidated balance sheets as goodwill. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired.

Goodwill is tested for impairment at the reporting unit level (operating segment or one level below an operating segment) on an annual basis (October 1 for us) and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. These events or circumstances could include a significant change in stock prices, business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

## **Table of Contents**

Application of the goodwill impairment test requires judgment, including the identification of reporting units, assignment of assets and liabilities to reporting units, assignment of goodwill to reporting units, and determination of the fair value of each reporting unit. The fair value of each reporting unit is estimated using a discounted cash flow methodology of income approach. This analysis requires significant judgments, including estimation of future cash flows, which is dependent on internal forecasts, estimation of the long-term rate of growth for our business, estimation of the useful life over which cash flows will occur, and determination of our weighted average cost of capital. The estimates used to calculate the fair value of a reporting unit change from period to period based on operating results and market conditions. Changes in these estimates and assumptions could materially affect the determination of fair value and goodwill impairment for the reporting unit. In addition, market approach is also adopted for fair value estimation.

In prior periods, including the period of our annual impairment test date, October 1, we believed the decline in our market capitalization triggered an impairment test. The determination of the fair value of a reporting unit is based on a market participant's perspective and therefore we utilized the income approach methodology of valuation, which we have consistently applied, to determine the fair value of our sole reporting unit using market participant assumptions. In the fourth quarter of 2012, the results of our impairment testing using the income approach did not result in the carrying amount of our reporting unit exceeding its fair value. We considered the market approach methodology but did not regard the market approach methodology of valuation as being a more reliable indicator of our fair value, in part because of the process we were engaged in relating to a strategic transaction such as the Merger and the market dislocation for China-based U.S. public companies. For example, in the fourth quarter of 2012, we received preliminary offers to acquire us at different prices and with different material terms and outstanding contingencies, which included financing.

In the first quarter of 2013, management updated its financial projections which were lower than previously forecasted. Given the decline in projections and the carrying amount of our sole reporting unit exceeding our market capitalization, we performed an interim goodwill impairment test using the income approach which did not result in the carrying amount of our reporting unit exceeding its fair value for the three month period ended March 31, 2013.

In the second quarter of 2013, the Special Committee continued to evaluate strategic alternatives for us, such as continuing as an independent company with or without a leveraged recapitalization, a share buyback or declaration of a special dividend. During this period our operating environment began to deteriorate as evidenced by a decrease in current and projected growth rates for the China gross domestic product, compared to historical growth rates, and continued uncertainty of government policies for the telecommunications and internet industries which changed market participant valuation assumptions including discount rates. On May 12, 2013, upon the unanimous recommendation of the Special Committee of our board of directors and the approval of our board of directors, we entered into the Merger Agreement. The \$12.00 per share Merger consideration set forth in the Merger Agreement would value us at approximately \$897 million. In management's judgment, the valuation represented the fair value of our reporting unit in assessing goodwill impairment considering the aforementioned factors. Because the fair value of the reporting unit was less than its carrying amount, we performed the second step of the interim test for goodwill impairment in the second quarter of 2013.

We performed the second step of the impairment test to determine the implied fair value of goodwill for the reporting unit, which requires us to allocate the fair value of the reporting unit to all of the assets and liabilities including any unrecognized intangible assets of the reporting unit. Based on the results of the impairment test, we recognized a loss on impairment of goodwill of \$287 million in the three months ended June 30, 2013.

**Table of Contents**

***Property and equipment, net*** Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated using the straight-line method over the estimated useful lives as follows:

Furniture, fixtures and electronic equipment	5 years
Motor vehicles	5 years
Leasehold improvements	Shorter of the lease term or 5 years
Software	3 years
Building	20 to 47 years
Self-constructed building improvements	10 years

Construction in progress primarily represents the cost to build the property and equipment. In addition to cost under the construction contracts and external cost directly related to the construction of such property and equipment, including equipment installation and shipping costs, are capitalized. Depreciation is recorded when the property and equipment are ready for their intended use. As of June 30, 2013, the construction in progress was \$18 million.

---

**Table of Contents**

**Impairment of long-term and short-term investments.** We review our long-term and short-term investments for other-than-temporary impairment in accordance with relevant accounting literature, based on the specific identification method. We consider available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds the investment's fair value, we consider, among other factors, general market conditions, government economic plans, the duration and the extent to which the fair value of the investment is less than the cost, and our intent and ability to hold the investment. In view of the declines of fair value below the carrying cost of certain short-term and long-term investments, we performed an evaluation to determine whether any of the declines were other-than-temporary. We determined that there were no fair value declines in long-term and short-term investments, and thus made no provision for impairment losses, in the second quarter of 2013 and 2012, respectively.

**Consolidated Results of Operations**

**Revenues.** Total revenues were \$140.2 million for the three-month period ended June 30, 2013, representing an 11.0% increase over the same period in 2012 and a 2.0% decrease sequentially. The year-over-year increase was primarily the result of healthy demand from China's telecom carriers and the sequential decrease was mainly due to the fluctuation of third party hardware revenues.

Software products and solutions revenue was \$127.6 million for the three-month period ended June 30, 2013, representing an increase of 9.2% over the comparable period in 2012 and a 1.5% sequential decrease. The year-over-year increase was primarily attributable to a 30.3% increase in revenue from China Unicom and an 18.7% increase in revenue from China Telecom. The sequential decrease was primarily attributable to a 5.2% decrease in revenue from China Unicom and a 1.9% decrease in revenue from China Mobile.

Service revenue was \$8.9 million for the three-month period ended June 30, 2013, representing an increase of 18.0% over the comparable period in 2012 and a 51.9% sequential increase. The sequential increase was primarily attributable to a 76.6% increase in revenue from China Mobile and a 43.5% increase in revenue from China Telecom.

Third-party hardware revenue was \$3.7 million for the three-month period ended June 30, 2013, representing a year-over-year increase of 92.5% and a sequential decrease of 51.3%. Third-party hardware revenue is not our business focus and represented 2.7% of our total revenues for the three-month period ended June 30, 2013.

During the second quarter of 2013, sales to our top three customers, China Mobile, China Unicom and China Telecom (and their respective provincial subsidiaries), accounted for approximately 95.8% of our total revenue.

**Cost of revenues.** Our cost of revenues was \$87.8 million for the three-month period ended June 30, 2013, representing an increase of 13.1% over the comparable period in 2012. Cost of revenues for the three-month period ended June 30, 2013 decreased 6.0% compared to the preceding quarter. The year-over-year increase in cost of revenues was primarily attributable to an increase in employee welfare, and headcount of approximately 975 implementation engineers for the period. The sequential decrease was mainly due to a reduction in domestic delivery costs and the reclassification of a number of delivery engineers as R&D engineers.

**Gross profit margin.** Our gross profit margin for the three-month period ended June 30, 2013 was 37.4%, compared to 38.5% in the comparable period in 2012 and 34.7% in the preceding quarter. The year-over-year decrease in gross margin was primarily attributable to an increase in employee welfare and headcount of approximately 975 implementation engineers, and the sequential increase was primarily due to a reduction in domestic delivery costs and the reclassification of a number of delivery engineers as R&D engineers.

**Table of Contents**

**Operating expenses.** Our operating expenses were \$335.8 million for the three-month period ended June 30, 2013, representing an increase of 619.6% over the comparable period in 2012 and 619.1% sequentially. The year-over-year and sequential increases were mainly due to the impairment of goodwill. Excluding the effects of the impairment of goodwill, the year-over-year and sequential increase in total operating expenses were mainly due to increases in sales and marketing and R&D expenses.

Sales and marketing expenses were \$20.3 million for three-month period ended June 30, 2013, representing an increase of 10.1% over the comparable period in 2012 and 9.1% sequentially. Both the year-over-year and sequential increases were mainly attributable to a combination of an increase in employee welfare and benefits and third-party professional fees of approximately US\$2.1 million.

General and administrative expenses were \$6.7 million for the three-month period ended June 30, 2013, representing a decrease of 14.6% over the comparable period in 2012 and a sequential decrease of 19.0%. The year-over-year decrease was mainly the result of a \$1.1 million decrease of bad debt expenses. The sequential decrease was mainly the result of a \$1.5 million decrease of bad debt expenses.

R&D expenses were \$22.3 million for the three-month period ended June 30, 2013, representing an increase of 9.2% over the comparable period in 2012 and a 12.3% sequential increase. The increased expenses reflect the addition of R&D engineers as we invested in product development for current and anticipated expansion outside of China, product standardization and delivery improvements. The sequential increase in research and development was mainly due to the temporary assignment of delivery engineers into R&D teams.

In the second quarter of 2013, we received government subsidies of \$0.3 million. We did not receive government subsidies in the first quarter of 2013 or in the year-ago period.

In the second quarter of 2013, the Company recognized a \$286.8 million impairment of goodwill, which was the result of the Company's periodic impairment review based on a number of factors and market conditions, including changing conditions in the IT sector in China and projections regarding the country's gross domestic product growth.

**Other income, net.** Other income, including interest income, dividend income, gain from sales of short-term investments, loss on disposal of variable interest entities, net of other expenses, was \$2.7 million for the three-month period ended June 30, 2013, representing an increase of 33.2% over the comparable period in 2012 and an increase of 19.4% sequentially. The year-over-year decrease was primarily due to decreases in dividend income and other income. The sequential increase was mainly due to an increase in gain from sales of short-term investments.

**Net loss.** Net loss was \$282.2 million for the three-month period ended June 30, 2013, compared to net income of \$5.3 million from the year-ago period and net income of \$12.7 million from the first quarter of 2013. Other than the effects of impairment of goodwill, the sequential decrease was primarily due to the recognition of Key Software Enterprise tax status for two of our Chinese subsidiaries, retroactively granted for the years 2011 and 2012, which resulted in a positive impact of \$9.0 million, or \$0.12 per basic share, and led to a tax benefit of \$6.6 million, or \$0.09 per basic share, which was recognized in the first quarter of 2013.

**Net (loss) income attributable to AsiaInfo-Linkage, Inc.** Net loss attributable to AsiaInfo-Linkage, Inc. for the three-month period ended June 30, 2013 was \$281.5 million, or \$3.87 per basic share, compared to net income of \$6.2 million, or \$0.09 per basic share, for the comparable period in 2012, and net income of \$14.1 million, or \$0.19 per basic share, for the previous quarter.

**Liquidity and Capital Resources**

Our liquidity and capital resources are provided mainly from cash collection from customers resulting from our core operating activities. Our capital requirements are primarily working capital requirements related to hardware sales and costs associated with the expansion of our business, such as research and development and sales and marketing expenses. We recognize hardware costs in full upon delivery of the hardware to our customers. In order to minimize our working capital requirements, we generally obtain from our hardware vendors payment terms that are timed to permit us to receive payment from our customers for the hardware before our payments to hardware vendors are due. With respect to our billing cycle, we generally require our customers to pay 80% to 90% of the invoice value of the hardware upon delivery. We typically place orders for hardware against back-to-back orders from customers and seek favorable payment terms from hardware vendors. However, we sometimes obtain less favorable payment terms from our customers, thereby increasing our working capital requirements. In addition to this careful management of our billing cycle, we have also historically financed working capital and other capital requirements through private placements of equity securities, our initial public offering in 2000 and, to a limited extent, bank loans.

---

**Table of Contents**

On December 4, 2009, we executed the Business Combination Agreement to combine our business with the business of Linkage through our acquisition of 100% of the outstanding share capital of Linkage Technologies, and we completed the combination with Linkage on July 1, 2010.

We had cash and cash equivalents, restricted cash and short-term investment totaling \$331.4 million as of June 30, 2013 as compared to \$353.8 million as of December 31, 2012. The decrease was mainly a result of our negative operating cash flow during the period.

Our net cash used in operating activities for the six-month period ended June 30, 2013 was \$21.3 million, which reflected our net loss of \$269.5 million adjusted by net non-cash related expenses, such as amortization, depreciation, impairment of goodwill, and stock-based compensation expenses etc., totalling of \$312.2 million and a net increase in the components of our working capital of \$64.0 million. Accounts receivable as of June 30, 2013 was \$341.9 million, consisting of \$143.8 million in billed receivables and \$198.1 million in unbilled receivables. Our billed receivables are recorded based on agreed-upon milestones included in our customer contracts.

Our days of sales outstanding, or DSO, as of June 30, 2013 was 156 days, which was a increase from 154 days as of June 30, 2012 and an increase from 144 days as of December 31, 2012. When calculating our DSO, we have adjusted for the net effect of the IBM-Type Arrangements. The increase in DSO from December 31, 2012 to June 30, 2013 was primarily attributable to a \$56.2 million increase in accounts receivable compared to December 31, 2012, which mainly reflects the business trend of our customers paying amounts due at the end of the year. Our DSO is impacted by a variety of factors that impact customer payment cycles, including the outcome of customer negotiations regarding payment terms, the relative maturity of the Customer Relations Management, Billing, Business Intelligence or other technology involved in a particular project, the systems used by the customer, geographic region, the scale of the project, and other factors. In addition, in a year we typically perform thousands of contracts for dozens of customers (comprising the major telecom carriers in the PRC and their provincial subsidiaries), and the payment terms of each contract can vary based on these factors.

Income taxes recoverable as of June 30, 2013 was \$2.5 million, which reflected the 10% preferential tax rate granted to AIBJ for its 2011 KSE status, which was not refunded by tax bureau as of June 30, 2013.

Our net cash used in investing activities for the six-month period ended June 30, 2013 was \$3.0 million. This was primarily due to the purchase of held to maturity securities for \$12.9 million, the purchase of property, plant and equipment for \$7.4 million and a \$3.1 million purchase of long-term investments, which was partially offset by \$19.9 million in proceeds from our sales of short-term investments.

Our net cash provided by financing activities for the six-month period ended June 30, 2013 was \$0.7 million, primarily due to proceeds from the exercise of stock options.

As of June 30, 2013, we had total credit facilities of \$152.1 million for working capital purposes, expiring on various dates up to April 2014, which were secured by bank deposits of \$33.9 million. As of June 30, 2013, unused credit facilities were \$124.3 million and used facilities totaled \$27.8 million. The used facilities were pledged as security for issuing standby letters of credit, borrowing of short-term bank loans and accounts payable to hardware suppliers and customers. Additional bank deposits of \$5.5 million were used for issuing standby letters of credit and bank acceptance drafts as of June 30, 2013. Total bank deposits pledged as security for credit facilities, standby letters of credit, short-term bank loans and bank acceptance drafts totaled \$39.4 million as of June 30, 2013 and were presented as restricted cash in our consolidated balance sheets. During the three-month period ended June 30, 2013, the largest aggregate amount that we had used of our credit facilities was \$27.8 million.



## **Table of Contents**

In May 2011, we entered into a land use right transfer agreement with the Beijing Municipal Bureau of Land and Resources pursuant to which we would acquire a land use right with a 50-year term, for a consideration of approximately \$3.0 million, which was paid in June and August 2011. Pursuant to the agreement, we have committed a minimum of \$17.9 million for capital expenditures to the building construction project, to commence construction by April 30, 2012, and to complete construction by April 30, 2014.

We anticipate that our available funds and cash flows provided by operations will be sufficient to meet our anticipated needs for working capital, capital expenditures for building construction and business expansion considering overseas projects purchase through 2013. We may need to raise additional funds in the future, however, in order to fund acquisitions, develop new or enhanced services or products, respond to competitive pressures to compete successfully for larger projects involving higher levels of hardware purchases, or if our business otherwise grows more rapidly than we currently predict. We anticipate that we would raise additional funds, if necessary, through new issuances of equity or debt securities, or through credit facilities extended by lending institutions.

Under PRC laws and regulations, our PRC subsidiaries are, and our former PRC VIEs were, subject to certain restrictions with respect to paying dividends or otherwise transferring a portion of their net assets to us. The amounts restricted include the paid-in capital and the statutory reserve. The aggregate amounts of capital and statutory reserves restricted and not available for distribution was \$76.2 million and \$88.9 million (10.0% and 8.7% of net assets) as of June 30, 2013 and December 31, 2012, respectively.

Furthermore, cash transfers from our PRC subsidiaries to our subsidiaries outside of China are subject to PRC government control of currency conversion. Shortages in the availability of foreign currency may restrict the ability of our PRC subsidiaries and VIEs to remit sufficient foreign currency to pay dividends or make other payments to us, or otherwise satisfy their foreign currency denominated obligations.

## **Off-Balance Sheet Arrangements**

We have not entered into any transactions, agreements or other contractual arrangements to which an entity unconsolidated with us is a party and under which we have (i) any obligation under a guarantee, (ii) any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity, (iii) any obligation under derivative instruments that are indexed to our shares and classified as equity in our consolidated balance sheets, or (iv) any obligation arising out of a variable interest in any unconsolidated entity that provides financing, liquidity, market risk or credit support to us or engages in leasing, hedging or research and development services with us.

As of June 30, 2013, we had credit facilities for working capital purposes totaling \$152.1 million, expiring on various dates up to April 2014, of which \$27.8 million had been used as security for issuing standby letters of credit, borrowing of short-term bank loans, and accounts payable to hardware suppliers and customers. Unused credit facilities were \$124.3 million. Total bank deposits pledged as security for credit facilities, standby letters of credit, short-term bank loans and bank acceptance drafts totaled \$39.4 million as of June 30, 2013 and were presented as restricted cash in the consolidated balance sheets.

As of June 30, 2013, we had outstanding standby letters of credit in the amount of \$23.3 million. They were used for performance guarantees amounting to \$21.1 million with respect to our performance on certain customer projects, and guarantees amounting to \$2.2 million with respect to future payments for building construction.

---

**Table of Contents**
**Accounting Pronouncements*****Newly adopted accounting pronouncements***

In December 2011, the Financial Accounting Standard Board, or FASB, issued an authoritative pronouncement related to disclosures about offsetting assets and liabilities. The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. In January 2013, the FASB further clarifies that ordinary trade receivables and receivables are not in the scope of the authoritative pronouncement and the pronouncement applies only to derivatives, repurchase agreements and reverse purchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria contained in the FASB Accounting Standards Codification or subject to a master netting arrangement or similar agreement. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The adoption of this guidance did not have a significant effect on our consolidated financial statements.

In February 2013, the FASB issued an authoritative pronouncement related to reporting of amounts reclassified out of accumulated other comprehensive income, to improve the transparency of reporting these reclassifications. Other comprehensive income includes gains and losses that are initially excluded from net income for an accounting period. Those gains and losses are later reclassified out of accumulated other comprehensive income into net income. The guidance does not change the current requirements for reporting net income or other comprehensive income in financial statements.

The new guidance will require an organization to:

Present (either on the face of the statement where net income is presented or in the notes) the effects on the line items of net income of significant amounts reclassified out of accumulated other comprehensive income but only if the item reclassified is required under US GAAP to be reclassified to net income in its entirety in the same reporting period.

Cross-reference to other disclosures currently required under US GAAP for other reclassification items (that are not required under US GAAP) to be reclassified directly to net income in their entirety in the same reporting period. This would be the case when a portion of the amount reclassified out of accumulated other comprehensive income is initially transferred to a balance sheet account (e.g., inventory for pension-related amounts) instead of directly to income or expense.

The guidance applies to all public and private companies that report items of other comprehensive income. Public companies are required to comply with the guidance for all reporting periods (interim and annual) effective for reporting periods beginning after December 15, 2012. Early adoption is permitted. We adopted this guidance on January 1, 2013 and have presented the relevant details in the notes to the financial statements.

***Recent accounting pronouncements not yet adopted***

In February 2013, the FASB issued an authoritative pronouncement related to obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed at the reporting date. The guidance addresses for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this pronouncement is fixed at the reporting date, except for obligations addressed within existing guidance in US GAAP. The guidance requires an entity to measure those obligations as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance also requires an entity to disclose the nature and amount of the obligation as well as other information about those obligations. The guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. The guidance should be applied retrospectively to all prior periods presented for those obligations resulting from joint and several liability arrangements within the scope that exist at the beginning of an entity's fiscal year of adoption. An entity may elect to use hindsight for the comparative periods (if it changed its accounting as a result of adopting the guidance in this pronouncement) and should disclose that fact. Early adoption is permitted. We are in the process of evaluating the effect of adoption of this guidance on our consolidated financial statements.

## **Table of Contents**

In March 2013, the FASB issued an authoritative pronouncement related to parent's accounting for the cumulative translation adjustment upon derecognition of certain subsidiaries or groups of assets within a foreign entity or of an investment in a foreign entity. When a reporting entity (parent) ceases to have a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business (other than a sale of in substance real estate or conveyance of oil and gas mineral rights) within a foreign entity, the parent is required to release any related cumulative translation adjustment into net income. Accordingly, the cumulative translation adjustment should be released into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided.

For an equity method investment that is a foreign entity, the partial sale guidance still applies. As such, a pro rata portion of the cumulative translation adjustment should be released into net income upon a partial sale of such an equity method investment. However, this treatment does not apply to an equity method investment that is not a foreign entity. In those instances, the cumulative translation adjustment is released into net income only if the partial sale represents a complete or substantially complete liquidation of the foreign entity that contains the equity method investment.

Additionally, the guidance clarifies that the sale of an investment in a foreign entity includes both: (1) events that result in the loss of a controlling financial interest in a foreign entity (i.e., irrespective of any retained investment); and (2) events that result in an acquirer obtaining control of an acquiree in which it held an equity interest immediately before the acquisition date (sometimes also referred to as a step acquisition). Accordingly, the cumulative translation adjustment should be released into net income upon the occurrence of those events.

The guidance is effective prospectively for fiscal years (and interim reporting periods within those years) beginning after December 15, 2013. The guidance should be applied prospectively to derecognition events occurring after the effective date. Prior periods should not be adjusted. Early adoption is permitted. If an entity elects to early adopt the guidance, it should apply the guidance as of the beginning of the entity's fiscal year of adoption. We are in the process of evaluating the effect of adoption of this guidance on our consolidated financial statements.

In July 2013, the FASB issued a pronouncement which provides guidance on financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists.

The guidance state that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets.

The guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. Early adoption is permitted. The guidance should be applied prospectively to all unrecognized tax benefits that exist at the effective date. Retrospective application is permitted. We are in the process of evaluating the effect of adoption of this guidance on our consolidated financial statements.

---

**Table of Contents**

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to interest rate risk primarily associated with our cash and short-term investments. To date, we have not entered into any types of derivatives to hedge against interest rate changes. There have been no significant changes in our exposure to changes in interest rates for the quarter ended June 30, 2013. Our exposure to interest rate changes is limited as we do not have any material borrowings.

We are exposed to exchange rate risk in connection with the relative value of the U.S. dollar and the RMB. A majority of our revenues and expenses relating to hardware sales and the service and software components of our business are denominated in RMB. As of June 30, 2013, approximately 89.2%, or \$264.1 million, of our cash, cash equivalents and restricted cash were RMB-denominated and approximately 10.5%, or \$31.0 million, were U.S. dollar-denominated, and approximately 0.2%, or \$0.5 million, were Hong Kong dollar-denominated. As of that date, the rate of exchange quoted by the People's Bank of China was US\$1.00 = RMB6.1787. If the exchange rate were to increase by 10% to US\$1.00 = RMB6.7966, our net assets would potentially decrease by \$55.6 million. If the exchange rate were to decrease by 10% to US\$1.00 = RMB5.5608, our net assets would potentially increase by \$68.0 million.

The value of our shares may be affected by the foreign exchange rate between U.S. dollars and RMB because the value of our business is effectively denominated in RMB, while our shares are traded in U.S. dollars. Furthermore, an increase in the value of the RMB may require us to exchange more U.S. dollars into RMB to meet the working capital requirements of our subsidiaries and VIEs in China. In addition, as we pursue our global strategy, we settle transactions denominated in various currencies of Southeast Asian countries, expect to continue to do so in future, and expect that such activities may create similar foreign exchange risk associated with the currencies of these jurisdictions. Depreciation of the value of the U.S. dollar will also reduce the value of the cash we hold in U.S. dollars, which we may use for purposes of future acquisitions or other business expansion. We actively monitor our exposure to these risks and adjust our cash position in the RMB and the U.S. dollar when we believe such adjustments will reduce our foreign exchange risk and are otherwise appropriate. We did not engage in any significant foreign exchange transactions during the three-month period ended June 30, 2013.

As in any other business, we are subject to the risk of macroeconomic changes such as recessions and inflation.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 under the Exchange Act, as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective.

**Changes in Internal Control over Financial Reporting**

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents**

**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

In October 2012, a putative stockholder of ours filed a civil action, derivatively on behalf of us, against the members of our Board of Directors and certain officers, which has been docketed as *Halpert v. Zhang, et al.*, in the United States District Court for the District of Delaware. The plaintiff asserted claims for breach of fiduciary duty, corporate waste, and unjust enrichment in connection with grants of stock options allegedly made in an amount that violated purported limitations set forth in the 2011 Stock Incentive Plan. The plaintiff requested rescission of the option grants in question, an award of unspecified damages to us, certain other equitable and injunctive relief, and an award of plaintiff's costs and disbursements, including legal fees. In January 2013, we and the individual defendants filed a motion to dismiss the action, and briefing on the motion was filed in March and April 2013.

Since our announcement that we entered into the Merger Agreement, certain alleged Company stockholders have filed three putative class actions against us, the members of our board of directors and Merger Sub in the Delaware Court of Chancery, under the captions *Guanghui Cai v. AsiaInfo-Linkage, Inc., et al.*, C.A. No. 8583-VCP, *Dawan Liu v. AsiaInfo-Linkage, Inc., et al.*, C.A. No. 8634-VCP, and *Loren Lowry v. AsiaInfo-Linkage, Inc., et al.*, C.A. No. 8695-VCP. Plaintiffs allege that our board of directors breached their fiduciary duties to our stockholders by favoring Parent over other potential purchasers, favoring their own interests over the interests of our stockholders, failing to take appropriate steps to maximize the value of the Company to our stockholders, agreeing to preclusive deal protection devices and otherwise agreeing to sell the Company for an unfairly low price. Plaintiffs further allege that the Company and Merger Sub aided and abetted those alleged breaches of fiduciary duty. Plaintiffs have requested an injunction, rescission of the Merger to the extent consummated, money damages if the Merger is consummated, certain other equitable relief, and an award of plaintiffs' costs, including legal fees. Plaintiffs in the *Liu* action have also requested a declaration that the merger is unfair, unjust and inequitable.

While we cannot guarantee the outcome of these proceedings, we believe that the final results will not have a material effect on our consolidated financial condition, results or operations, or cash flows.

**ITEM 6. EXHIBITS**

Please see Exhibit Index.

**Table of Contents**

**SIGNATURE**

Pursuant to the requirements of the Securities Exchange Act of 1934, AsiaInfo-Linkage, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

AsiaInfo-Linkage, Inc.

Date: August 9, 2013

By: */s/ Jun Wu*

Name: Jun Wu

Title: Executive Vice President and Chief Financial Officer  
(signing on behalf of the registrant and as principal financial officer)

**Table of Contents****EXHIBIT INDEX**

The following exhibits are filed as a part of this Report.

Exhibit No.	Exhibit Title	Filed Herewith	Form	Incorporated by Reference File		Filing Date
				Exhibit No.	No.	
10.1	Agreement and Plan of Merger among Skipper Limited, Skipper Acquisition Corporation, and AsiaInfo-Linkage, Inc.		8-K	2.1	001-15713	5/13/13
10.2	Limited Guarantee of Power Joy (Cayman) Limited		8-K	10.1	001-15713	5/13/13
10.3	Limited Guarantee of CITIC Capital MB Investment Limited		8-K	10.2	001-15713	5/13/13
10.4	Limited Guarantee of CPEChina Fund, L.P.		8-K	10.3	001-15713	5/13/13
10.5	Limited Guarantee of InnoValue Capital Ltd.		8-K	10.4	001-15713	5/13/13
10.6	Limited Guarantee of CBC TMT III Limited		8-K	10.5	001-15713	5/13/13
10.7	Limited Guarantee of Ellington Investment Pte. Ltd.		8-K	10.6	001-15713	5/13/13
10.8	Letter Agreement with Steve Zhang regarding Employment Agreement Amendment and Extension		8-K	10.1	001-15713	5/21/13
10.9	Letter Agreement with Jun (Michael) Wu regarding Employment Agreement Amendment and Extension		8-K	10.2	001-15713	5/21/13
10.10	Letter Agreement with Guoxiang Liu regarding Employment Agreement Amendment and Extension		8-K	10.3	001-15713	5/21/13
10.11	Employment Contract Amendment Agreement with Yadong Jin		8-K	10.4	001-15713	5/21/13
31.1	Certification of Principal Executive Officer required by Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated August 9, 2013	X				
31.2	Certification of Principal Financial Officer required by Rules 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated August 9, 2013	X				
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated August 9, 2013	X				
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated August 9, 2013	X				
101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) Condensed Consolidated Statements of Operations for the three months and six months ended June 30, 2013 and 2012; (ii) Condensed Consolidated Statements of Comprehensive Income for the three months and six months ended June 30, 2013 and 2012; (iii) Condensed Consolidated Balance Sheets as of June 30, 2013 and December 31, 2012; (iv) Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2013 and 2012; (v) Condensed Consolidated Statements of Equity for the three months and six months ended June 30, 2013 and 2012; and (vi) Notes to Condensed Consolidated Financial Statements *					X

\* The interactive data files in Exhibit No. 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, and not filed for purposes of Section 18 of the Securities Exchange Act of 1934,

as amended, and otherwise are not subject to liability under those sections.