

China Digital TV Holding Co., Ltd.

Form 20-F

April 16, 2013

Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

**FORM 20-F**

.. **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

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

For the fiscal year ended December 31, 2012

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

OR

..

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

Date of event requiring this shell company report \_\_\_\_\_

Commission file number 001-33692

**CHINA DIGITAL TV HOLDING CO., LTD.**

(Exact Name of Registrant as Specified in Its Charter)

N/A

(Translation of Registrant's Name Into English)

Cayman Islands

(Jurisdiction of Incorporation or Organization)

Jingmeng High-Tech Building B, 4th Floor

No. 5 Shangdi East Road

Haidian District, Beijing 100085

People's Republic of China

(Address of Principal Executive Offices)

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(Name, Telephone, Email and/or Facsimile Number and Address of Company Contact Person)

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

| <b>Title of Each Class</b>                              | <b>Name of Each Exchange On Which Registered</b> |
|---|--|
| <b>Ordinary shares, par value US\$0.0005 per share*</b> | <b>New York Stock Exchange</b>                   |

**American depositary shares, each representing one ordinary share**

\* Not for trading, but only in connection with the listing on the New York Stock Exchange of American depositary shares, or ADSs, each representing one ordinary share.

**Securities registered or to be registered pursuant to Section 12(g) of the Act:**

**None**

(Title of Class)

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:**

**None**

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2012, 59,100,754 ordinary shares, par value US\$0.0005 per share, were issued and outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

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

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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer

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

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U.S. GAAP  International Financial Reporting Standards as issued

Other

by the International Accounting Standards Board

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

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

**Table of Contents**

**TABLE OF CONTENTS**

|  |     |
|--|-----|
| <b><u>INTRODUCTION</u></b>   | 1   |
| <b><u>FORWARD-LOOKING STATEMENTS</u></b>   | 1   |
| <b><u>PART I</u></b>   | 2   |
| Item 1. <u>Identity of Directors, Senior Management and Advisers</u>                         | 2   |
| Item 2. <u>Offer Statistics and Expected Timetable</u>                                       | 2   |
| Item 3. <u>Key Information</u>   | 3   |
| Item 4. <u>Information on the Company</u>  | 28  |
| Item 4A. <u>Unresolved Staff Comments</u>  | 50  |
| Item 5. <u>Operating and Financial Review and Prospects</u>                                  | 50  |
| Item 6. <u>Directors, Senior Management and Employees</u>                                    | 70  |
| Item 7. <u>Major Shareholders and Related Party Transactions</u>                             | 80  |
| Item 8. <u>Financial Information</u>   | 86  |
| Item 9. <u>The Offer and Listing</u>   | 87  |
| Item 10. <u>Additional Information</u>   | 89  |
| Item 11. <u>Quantitative and Qualitative Disclosures About Market Risks</u>                  | 93  |
| Item 12. <u>Description of Securities Other than Equity Securities</u>                       | 94  |
| <b><u>PART II</u></b>  | 96  |
| Item 13. <u>Defaults, Dividend Arrearages and Delinquencies</u>                              | 96  |
| Item 14. <u>Material Modifications to the Rights of Security Holders and Use of Proceeds</u> | 96  |
| Item 15. <u>Controls and Procedures</u>  | 96  |
| Item 16A. <u>Audit Committee Financial Expert</u>  | 98  |
| Item 16B. <u>Code of Ethics</u>  | 98  |
| Item 16C. <u>Principal Accountant Fees and Services</u>                                      | 99  |
| Item 16D. <u>Exemptions from the Listing Standards for Audit Committees</u>                  | 99  |
| Item 16E. <u>Purchases of Equity Securities by the Issuer and Affiliated Purchasers</u>      | 99  |
| Item 16F. <u>Change in Registrant's Certifying Accountant</u>                                | 99  |
| Item 16G. <u>Corporate Governance</u>  | 100 |
| Item 16H. <u>Mine Safety Disclosure</u>  | 100 |
| <b><u>PART III</u></b>   | 100 |
| Item 17. <u>Financial Statements</u>   | 100 |
| Item 18. <u>Financial Statements</u>   | 100 |
| Item 19. <u>Exhibits</u>   | 100 |
| <b><u>EXHIBIT INDEX</u></b>  |     |

**Table of Contents**

**INTRODUCTION**

Except where the context otherwise requires and for purposes of this annual report only:

ADSs refers to our American depositary shares, each of which represents one ordinary share;

ADRs refers to American depositary receipts, which, if issued, evidence our ADSs;

CA systems refers to conditional access systems provided to the PRC's digital television market, which consist of: (1) smart cards that are inserted into set-top boxes at the subscriber's end, or terminal end; (2) software installed at the digital television network operator's transmission point, or head end; and (3) software for set-top boxes, enabling digital television network operators to control the distribution of contents and value-added services to their subscribers and block unauthorized access to their networks;

China or the PRC refers to the People's Republic of China, excluding, for the purposes of this annual report, Hong Kong, Macau and Taiwan;

RMB or Renminbi refers to the legal currency of China;

U.S. dollars or US\$ refers to the legal currency of the United States; and

U.S. GAAP refers to generally accepted accounting principles in the United States.

All references to CDTV Holding, we, us or our include China Digital TV Holding Co., Ltd., its subsidiaries, the businesses acquired from Novel-Tongfang Information Engineering Co., Ltd., or N-T Information Engineering, and, in the context of describing our operations and consolidated financial information, also include Beijing Novel-Super Digital TV Technology Co., Ltd. (formerly known as Beijing Novel-Tongfang Digital TV Technology Co., Ltd.), or N-S Digital TV, and its subsidiaries.

**FORWARD-LOOKING STATEMENTS**

This annual report contains 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, with respect to our business, operating results and financial condition as well as our current expectations, assumptions, estimates and projections about our industry. All statements other than statements of historical fact in this annual report are forward-looking statements. These forward-looking statements can be identified by words or phrases such as the words anticipate, believe, estimate, expect, intend, plan, may, is/are likely to, should, expressions. These forward-looking statements include, without limitation, statements relating to:

changes in technology standards in the digital television broadcasting industry and our ability to adapt to these changes;

our expectations regarding demand for our products and services;

our ability to develop new products and services, and expand our sales and distribution network and other aspects of our operations;

expected changes in our revenues and cost and expense items;

our ability to effectively protect our intellectual property rights as well as not infringe on the intellectual property rights of others;

the competitiveness of our products and services;

**Table of Contents**

the level of competition in the CA systems market;

government policies and regulations relating to the digital television broadcasting industry, the CA systems industry and other areas relevant to our business activities;

any significant changes to the PRC government's ongoing digitalization program;

general economic and business conditions in the PRC and elsewhere;

our future business development and economic performance;

our future business development plans and strategic initiatives; and

the future expansion of the PRC digital television broadcasting market, and factors driving that growth.

These forward-looking statements involve various risks and uncertainties. These forward-looking statements reflect our current views with respect to future events and are not a guarantee of future performance. Actual results may differ materially from the information contained in the forward-looking statements as a result of a number of factors, including, without limitation, the risk factors set forth in Item 3. Key Information "D. Risk Factors" and the following:

general economic and business conditions in the PRC and elsewhere;

governmental, statutory, regulatory or administrative initiatives affecting us;

trends in the PRC's digital television broadcasting industry, including progress of digitalization in the PRC and the growth of digital television network operators;

future profitability of our business and operations;

exchange rate fluctuations between the Renminbi and other currencies; and

the availability of qualified management and technical personnel.

Due to these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this annual report might not occur in the way we expect, or at all. Accordingly, you should not place undue reliance on any forward-looking information. The forward-looking statements made in this annual report relate only to events or information as of the date on which the statements are made in this annual report. We undertake no obligation to update or otherwise revise the forward-looking statements in this annual report, whether as a result of new information, future events or otherwise.

**PART I**

**Item 1. Identity of Directors, Senior Management and Advisers**

Not Applicable.

**Item 2. Offer Statistics and Expected Timetable**

Not Applicable.

**Table of Contents****Item 3. Key Information****A. Selected Financial Data****Our Selected Consolidated Financial Data**

The following selected consolidated financial data should be read in conjunction with Item 5. Operating and Financial Review and Prospects and our audited consolidated financial statements and the notes thereto included elsewhere in this annual report on Form 20-F. The selected consolidated statement of operations data for the years ended December 31, 2010, 2011 and 2012, and the selected consolidated balance sheet data as of December 31, 2011 and 2012 set forth below are derived from our audited consolidated financial statements included elsewhere in this annual report. The selected consolidated statement of operations data for the years ended December 31, 2008 and 2009 and the selected historical consolidated balance sheet data as of December 31, 2008, 2009 and 2010 set forth below are derived from our audited consolidated financial statements which are not included in this annual report.

Our audited historical consolidated financial statements have been prepared and presented in accordance with U.S. GAAP.

Our historical results for any prior period do not necessarily indicate our results to be expected for any future period.

|   | For the years ended December 31,                                |               |               |                |               |
|---|---|---------------|---------------|----------------|---------------|
|   | 2008  | 2009          | 2010          | 2011           | 2012          |
|   | (In thousands of U.S. dollars, except share and per share data) |               |               |                |               |
| <b>Consolidated Statements of Operations Data:</b>                    |   |               |               |                |               |
| Revenues  |   |               |               |                |               |
| Products  |   |               | US\$          |                | US\$          |
| Services  | US\$ 64,412   | US\$ 49,146   | 82,518        | US\$ 95,162    | 85,319        |
|   | 6,285   | 5,918         | 5,225         | 5,378          | 4,925         |
| <b>Total revenues</b>   | <b>70,697</b>   | <b>55,064</b> | <b>87,743</b> | <b>100,540</b> | <b>90,244</b> |
| Business tax  | (363)   | (360)         | (620)         | (1,445)        | (1,501)       |
| <b>Net revenues</b>   | <b>70,334</b>   | <b>54,704</b> | <b>87,123</b> | <b>99,095</b>  | <b>88,743</b> |
| Cost of revenues  |   |               |               |                |               |
| Products  | 10,877  | 9,716         | 15,148        | 16,100         | 16,880        |
| Services  | 2,828   | 3,686         | 3,040         | 3,027          | 3,952         |
| <b>Total cost of revenues</b>   | <b>13,705</b>   | <b>13,402</b> | <b>18,188</b> | <b>19,127</b>  | <b>20,832</b> |
| <b>Gross profit</b>   | <b>56,629</b>   | <b>41,302</b> | <b>68,935</b> | <b>79,968</b>  | <b>67,911</b> |
| <b>Total operating expenses</b>                                       | <b>19,068</b>   | <b>20,775</b> | <b>25,325</b> | <b>35,240</b>  | <b>40,452</b> |
| <b>Income from operations</b>   | <b>37,561</b>   | <b>20,527</b> | <b>43,610</b> | <b>44,728</b>  | <b>27,459</b> |
| Interest income   | 9,138   | 6,070         | 5,294         | 6,810          | 6,318         |
| Interest expense  |   |               |               | (1,452)        | (739)         |
| Gain/(loss) from forward contracts                                    |   |               |               | 404            | (690)         |
| Impairment loss on long-term investments                              |   |               | (5,000)       |                | (4,487)       |
| Other (expense)/income  | (412)   | (65)          | (92)          | 594            | 549           |
| <b>Income before income taxes</b>                                     | <b>46,287</b>   | <b>26,532</b> | <b>43,812</b> | <b>51,084</b>  | <b>28,410</b> |
| Income tax expense  | 3,235   | 1,261         | 10,250        | 9,762          | 22,232        |
| <b>Net income before (loss)/income from equity method investments</b> | <b>43,052</b>   | <b>25,271</b> | <b>33,562</b> | <b>41,322</b>  | <b>6,178</b>  |
| (Loss)/income from equity method investments, net of income taxes     | (4)   | 20            | (151)         | (1,052)        | (640)         |
| <b>Net income</b>   | <b>43,048</b>   | <b>25,291</b> | <b>33,411</b> | <b>40,270</b>  | <b>5,538</b>  |

**Table of Contents**

|  | For the years ended December 31,                                |            |      |            |      |            |      |            |      |            |
|--|---|------------|------|------------|------|------------|------|------------|------|------------|
|  | 2008  |            | 2009 |            | 2010 |            | 2011 |            | 2012 |            |
|  | (In thousands of U.S. dollars, except share and per share data) |            |      |            |      |            |      |            |      |            |
| Net loss attributable to noncontrolling interest                                       |   | (14)       |      | (13)       |      | (10)       |      | (730)      |      | (1,389)    |
| Net income attributable to holders of ordinary shares                                  | US\$  | 43,062     | US\$ | 25,304     | US\$ | 33,421     | US\$ | 41,000     | US\$ | 6,927      |
| <b>Earnings per share data:</b>  |   |            |      |            |      |            |      |            |      |            |
| Net income per ordinary share basic  | US\$  | 0.75       | US\$ | 0.44       | US\$ | 0.57       | US\$ | 0.70       | US\$ | 0.12       |
| Net income per ordinary share diluted  | US\$  | 0.72       | US\$ | 0.43       | US\$ | 0.57       | US\$ | 0.69       | US\$ | 0.12       |
| Weighted average shares used in calculating basic net income per share ordinary shares |   | 57,138,985 |      | 57,728,009 |      | 58,313,467 |      | 58,934,912 |      | 59,011,396 |
| Weighted average shares used in calculating diluted net income per share               |   | 60,058,724 |      | 58,591,072 |      | 58,779,027 |      | 59,075,466 |      | 59,092,804 |
| <b>Consolidated Balance Sheet Data:</b>  |   |            |      |            |      |            |      |            |      |            |
| Cash and cash equivalents  | US\$  | 202,947    | US\$ | 131,087    | US\$ | 148,944    | US\$ | 201,557    | US\$ | 130,697    |
| Total assets   |   | 297,976    |      | 263,488    |      | 273,642    |      | 321,338    |      | 193,565    |
| Total liabilities  |   | 71,950     |      | 10,464     |      | 94,622     |      | 111,016    |      | 110,402*   |
| Total China Digital TV Holding Co., Ltd. shareholders equity                           |   | 224,462    |      | 253,024    |      | 178,500    |      | 206,442    |      | 80,458*    |
| Noncontrolling interest  |   | 1,564      |      |            |      | 520        |      | 3,880      |      | 2,705      |
| Total liabilities and equity   | US\$  | 297,976    | US\$ | 263,488    | US\$ | 273,642    | US\$ | 321,338    | US\$ | 193,565    |

\* The amount reflects an adjustment to dividend payable included in total liabilities and additional paid-in capital included in equity, respectively, in the amount of US\$971,377 to the amount reported in our unaudited financial results for the fourth quarter and full year ended December 31, 2012 announced on February 26, 2013 to rectify an error.

In November 2012, our board of directors declared a special cash dividend of US\$2.30 per ordinary share.

**Exchange Rate Information**

Our business is primarily conducted in China and substantially all of our revenues are denominated in Renminbi. We present our historical consolidated financial statements in U.S. dollars. In addition, solely for the convenience of the reader, this annual report contains translations of certain Renminbi amounts into U.S. dollars at specific rates. For January 1, 2009 and all later dates and periods, the exchange rate refers to the exchange rate as set forth in the H.10 statistical release of the Federal Reserve Board. Unless otherwise indicated, conversions of Renminbi into U.S. dollars in this annual report are based on the exchange rate on December 31, 2012. We make no representation that any Renminbi amounts could have been, or could be, converted into U.S. dollars or vice versa, as the case may be, at any particular rate, the rates stated below, or at all. For a detailed explanation of the risk of currency rate fluctuations, please see Risk Factors Risks Relating to the People's Republic of China Fluctuations in exchange rates could result in foreign currency exchange losses. The PRC government imposes controls over its foreign currency reserves in part through direct regulation of the conversion of Renminbi into foreign exchange and through restrictions on foreign trade.

On April 12, 2013, the daily exchange rate reported by the Federal Reserve Board was RMB6.1914 to US\$1.00. The following table sets forth additional information concerning exchange rates between Renminbi and U.S. dollars for the periods indicated. These rates are provided solely for your convenience and are not necessarily the exchange rates that we use in this annual report or will use in the preparation of our future periodic reports or any other information to be provided to you.

**Table of Contents**

|                                     | RMB per US\$1.00 |        |
|-------------------------------------|------------------|--------|
|                                     | High             | Low    |
| October 2012                        | 6.2877           | 6.2372 |
| November 2012                       | 6.2454           | 6.2221 |
| December 2012                       | 6.2502           | 6.2251 |
| January 2013                        | 6.2303           | 6.2134 |
| February 2013                       | 6.2438           | 6.2213 |
| March 2013                          | 6.2246           | 6.2105 |
| April 2013 (through April 12, 2013) | 6.2078           | 6.1914 |

The following table sets forth the average exchange rates between Renminbi and U.S. dollars for each of 2008, 2009, 2010, 2011 and 2012 calculated by averaging the exchange rates on the last day of each month during each of the relevant years.

**Average Exchange Rate**

|      | RMB per US\$ 1.00 |
|------|-------------------|
| 2008 | 6.9193            |
| 2009 | 6.8295            |
| 2010 | 6.7603            |
| 2011 | 6.4475            |
| 2012 | 6.2990            |

**B. Capitalization and Indebtedness**

Not Applicable.

**C. Reasons for the Offer and Use of Proceeds**

Not Applicable.

**D. Risk Factors**

*You should carefully consider all of the information in this annual report, including the risks and uncertainties described below, before deciding to invest in our ADSs. The trading price of our ADSs could decline due to any of these risks and uncertainties, and you may lose all or part of your investment.*

**Risks Relating to Our Business and Industry**

*The PRC television broadcasting industry may not digitalize as quickly as we expect, as a result of which our revenues and net income would be materially adversely affected.*

Our future success depends upon the pace at which PRC television network operators switch from analog to digital transmission. In particular, various factors, including those beyond our control, may cause PRC television network operators to convert from analog to digital transmission at a slower pace. Moreover, although the PRC government has strongly encouraged cable television network operators to digitalize their networks and has set a target of 2015 for all analog channels to be switched off (except for those required to be retained during the transition period), it may relax or cancel the 2015 target. The pace of digitalization may also be slowed down as a result of uncertainties in the change of industrial policies. In addition, PRC television viewers may fail to subscribe to digital television services in sufficient numbers to support wide-scale digitalization. PRC television network operators may also decide that the commercial benefits of digitalization are outweighed by the costs or other commercial or policy considerations. If any of these or other factors were to cause the pace of digitalization to proceed significantly more slowly than we anticipate, our sales of CA systems, in particular smart cards, would suffer significantly, and our revenues and net income would be materially reduced.

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**Table of Contents**

***Changes in the regulatory environment of, and government policies towards, the PRC television broadcasting industry could have a material adverse effect on our business, financial condition and results of operations.***

Strong PRC government support has been a significant driver of the PRC television broadcasting industry's transition from analog to digital transmission. Although the PRC government has set a target of 2015 for all cable television networks to switch to digital transmissions, terminating all analog transmissions except for up to six channels that will continue in service for the benefit of those unable to afford digital television, we cannot assure you that the government will not change or adjust its digitalization policies at any time, including canceling or relaxing the target for digitalization. If the digitalization process in the PRC were to be slowed down or otherwise adversely affected by any government action or inaction, we may not be able to develop new customers or attract new business from existing customers, and our growth and prospects would be materially and adversely affected.

Furthermore, the television broadcasting industry in the PRC is highly regulated. Government regulations with respect to television broadcasting content, the amount and content of advertising, the pricing of pay-television subscriptions, the role of private-sector investment and the role of foreign investment significantly influence the business strategies and operating results of our customers. For example, the PRC State Administration of Press, Publication, Radio, Film and Television (formerly, the PRC State Administration of Radio, Film and Television), or the SARFT, issues licenses without which our customers cannot operate, and may withdraw such licenses for violation of its regulations. Among other things, the SARFT must approve the creation of new premium content channels and has the power to order television network operators to stop airing programs or advertising that it considers illegal or inappropriate. Any adverse government actions against television network operators could in turn cause us to lose existing or potential customers.

In addition, many of our customers are directly or indirectly owned by the central PRC government or provincial or local governments. As a result, their business strategies and capital expenditure budgets are significantly influenced by government policies at various levels. Any change in the business strategies of our customers that leads to a reduction in the funds available to purchase our CA systems could have a material adverse effect on our business, financial condition and results of operations. Furthermore, the ongoing consolidation of the PRC cable television broadcasting industry could, among other things, substantially increase the bargaining power of the consolidated network operators over us and require us to reduce the prices of our CA systems and other products and services, which could, in turn, materially reduce our revenues and profitability.

***If significant numbers of television viewers in the PRC are unwilling to pay for digital television or related value-added services, our business and profits will suffer.***

The substantial majority of our revenues are derived from digital television network operators who purchase our head-end CA systems software and smart cards to insert in the set-top boxes of their subscribers. As a result, we are substantially dependent upon the television network operators' ability to sell digital television subscriptions to viewers. In addition, the success of our efforts to generate future revenues by offering value-added services to television viewers ultimately depends on whether viewers are willing to pay for such value-added services.

We cannot assure you that television network operators will be successful in promoting digital television or value-added services. In particular, television viewers in the PRC are accustomed to receiving television for free or at a very low price. Even viewers who are accustomed to paying for cable television subscriptions have historically paid very low rates and may not be willing to pay significantly higher rates for digital television services, or additional fees for value-added services. If digital television network operators are unable to develop unique and compelling content to differentiate from the content provided through analog transitions or offer value-added services that meet viewers' needs at an affordable price, these operators may find it difficult to persuade viewers to accept the pay-television model or pay more for digital television or value-added services than viewers have historically paid for analog television. In that event, our customers' digital subscriber numbers may not grow and we may be unable to sustain our current level of revenue, net income and/or growth.

## **Table of Contents**

***If large numbers of television network operators who have already installed our CA system head-end software do not purchase sufficient quantities of our smart cards, our financial condition and results of operations would be materially and adversely affected.***

Television network operators who purchase and install our CA systems head-end software generally purchase our smart cards in batches over a period from several months to several years as they roll out digital services to their subscribers in stages. Substantially all of our revenues are derived from the sale of smart cards to customers who are engaged in such service roll-outs. However, certain television network operators have installed our CA systems head-end software and subsequently failed to purchase sufficient quantities of our smart cards. Factors that may cause a television network operator to suspend or halt its digitalization using our products include, but are not limited to, changes in such television network operator's management priorities or financial condition, and a decision by such television network operator to carry out digitalization using the CA systems of a competitor.

In January 2010, the PRC government stepped up its policy to encourage convergence of television broadcasting, telecommunications and Internet services. Although this policy may lead to acceleration of the digitalization of cable networks as the cable operators prepare themselves for potential competition from telecommunications operators, it may also have a material adverse effect on our business. In particular, as a response to that policy, and as an important measure to strengthen the competitiveness of the cable television industry as a whole, the SARFT has increased its efforts to consolidate the cable television industry. As a result, provincial cable operators have gained increasing influence over the municipal cable operators, including the latter's purchase and investment decisions. If the provincial cable operators, who may be CA customers of our competitors or otherwise prefer our competitors' products, direct the municipal cable operators to suspend or cancel their orders for our smart cards or purchase smart cards from our competitors, our business could suffer.

Furthermore, the SARFT released a unified CA systems standard in March 2012, which requires a unified CA system that is compatible with different terminals developed by different vendors to be used. Although this standard has not yet been implemented, upon such implementation, it would allow television network operators greater flexibility in selecting vendors of CA systems and related upgrades, including those of our competitors.

If large numbers of television network operators who have already installed our CA systems head-end software fail to purchase commercial quantities of our smart cards, our financial condition and results of operations would be materially and adversely affected.

***We derive substantially all of our revenues from customers who are installing new CA systems, and if we are unable to continue attracting new customers to install our CA systems or persuade existing customers to purchase our system upgrades or value-added applications, our revenues, profitability and prospects may be materially and adversely affected.***

CA systems vendors in more mature digital television markets, such as the United States and Europe, derive revenues not only from the purchase of new CA systems by television network operators who are switching from analog to digital transmissions, but also from the purchase of new and replacement smart cards, system upgrades and new value-added services by existing customers. In the PRC, however, cable television network operators are still in the process of purchasing CA systems and introducing digital content and services to their subscribers. To date, none of our customers have made a follow-on purchase for system upgrades or card replacements. As a result, the success of our business depends primarily on our ability to attract a continuing stream of customers who are switching from analog to digital transmission. As the digitalization process in the PRC continues to progress in light of the targeted completion in the year 2015, the number of cable television network operators who have not switched from analog to digital transmission, who are the prospective customers of our CA systems, has decreased significantly. If we are unable to continue attracting sufficient numbers of such customers, or to develop a significant additional source of recurring revenues, our revenues and profitability may be materially reduced and our prospects may suffer.

***Our business will suffer if we do not respond effectively to technological or commercial changes in our industry.***

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**Table of Contents**

Our business and the market in which we operate are characterized by rapid commercial and technological change, evolving industry standards and frequent product enhancements. As digital broadcasting becomes more popular in the PRC, television network operators are likely to seek more sophisticated CA technology that offers them greater reliability, flexibility and functionality in delivering protected content or value-added services to viewers. As methods of distributing information and entertainment evolve, CA technology may also need to evolve to provide content protection for distribution platforms other than television. Our continued success will depend, in part, on our ability to develop and market products and services that respond to technological changes and evolving market demand or industry standards in a timely and cost-effective manner. We will need to invest significant financial resources in research and development to keep pace with technological advances in the CA systems industry and related industries. However, research and development activities are inherently uncertain, and our significant expenditures on research and development may not yield corresponding benefits. If we fail to develop and introduce products and services that effectively respond to technical changes and evolving market demand or industry standards and compete effectively with products and services offered by our competitors, our sales may be significantly reduced and our revenues and profitability will suffer.

***We depend, and expect to continue to depend, on a limited number of customers for a significant portion of our revenues in any single period. If one customer defers or cancels its orders or chooses our competitors' products or services, our revenues and net income could decline significantly.***

The revenues generated by our top five customers for a particular year as a percentage of our total revenues declined from 48.3% in 2006 to 21.0% in 2012. However, we currently still derive, and we expect to continue to derive, a significant portion of our revenues from a limited number of customers, although the particular customers may vary from period to period. As digital cable television systems are still at the developing stage in the PRC, the largest shipments of smart cards tend to be to operators who are launching new digital transmission systems and need to purchase in bulk for their established networks. If a customer significantly reduces the volume of its purchases from us, defers or cancels orders or terminates its relationship with us, our revenues and net income could decline significantly and, as a result, our financial condition and results of operations could be materially and adversely affected.

***Our business may suffer if cable television network operators, who currently comprise our primary customer base, do not compete successfully with existing and emerging alternative platforms for delivering television programs, including terrestrial networks, Internet protocol television, mobile television and satellite broadcasting networks.***

Our existing customers are mainly cable television network operators in the PRC, which compete with traditional terrestrial television networks for the same pool of viewers. As technologies develop, other means of delivering information and entertainment to television viewers are evolving. For example, some telecommunications companies in the PRC are seeking to compete with terrestrial broadcasters and cable television network operators by offering Internet protocol television, or IPTV, which allows telecommunications companies to stream television programs through telephone lines. The SARFT has officially issued seven IPTV licenses and seven Internet TV licenses, and it may issue significantly more IPTV and Internet TV licenses in the future. The SARFT also issued a broadcast license in 2006 to the PRC's first direct satellite broadcast company, which began operation in 2008. Since 2009, a television operator has started to offer mobile television services. We may not be as successful in selling our CA systems to the operators of IPTV, or terrestrial, satellite or mobile television networks as we have been in selling to cable television network operators. To the extent that the terrestrial television networks, telecommunications companies or satellite television network operators compete successfully with cable television network operators for viewers, the ability of our existing cable customer base to attract and retain subscribers may be adversely affected. As a result, demand for additional smart cards could falter and our business, financial condition and results of operations would be materially and adversely affected.

***Our business could be harmed if the security of our customers' networks is compromised due to the failure of our CA systems or the security breach of the software or hardware supplied by other vendors.***

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**Table of Contents**

We face risks relating to the failure of our CA systems to block unauthorized access to the television networks of our customers. Our CA systems use a combination of signal scrambling and encryption to prevent unauthorized viewing of our customers' television programs. An important component of our CA systems is the smart cards we provide for our customers' individual subscribers. Unauthorized viewing and use of content could be accomplished by counterfeiting our smart cards, stealing our system's authorization messages or security codes, or in any other way thwarting our CA systems' security features. Any significant security breach could require us to develop and implement solutions that could be costly or time-consuming, or to replace an operator's smart cards at our own expense. For example, pursuant to our contracts with buyers of our CA systems, if we were unable to remedy such security breach with system modifications, we could be obligated to replace the cards free of charge if the breach occurs within the first year (or in some cases, within the first two or three years) after the sale. Even though we have not experienced any significant counterfeiting or other security breach, we cannot assure you that our current assumptions regarding the security of our CA systems are reasonable. We could be obligated to incur a significant portion of the cost of replacing our smart cards in future years if any significant counterfeiting or security breach occurs. See Item 4. Information on the Company B. Business Overview Our Products and Services CA Systems. The cost of smart card replacement and the damage to our reputation could have a material adverse effect on our business, financial condition and results of operations.

In addition to our CA systems, the secured transmission of digital television programming also relies on certain other software and hardware components, such as set-top boxes supplied by other vendors, used on our customers' digital television networks. A security breach of any of these other software and hardware components could also result in unauthorized access to the television networks of our customers. For example, in November 2007, it was discovered that an individual located in the city of Daqing in Heilongjiang Province had provided shared access to the local digital television network to over 100 other persons without authorization by hacking into certain set-top boxes used on that network, which do not have advanced security features due to cost considerations. By using a tracking technology offered by our CA systems, which enables an operator to track down the compromised set-up boxes, the local television network operator identified the points of breach, took measures to block further unauthorized access and contained the impact of the breach. The perpetrator was convicted and sentenced to eight months in prison. We believe we are not liable for such security breach of software or hardware components that are supplied by other vendors under the terms of our contractual arrangements. However, our business, financial conditions and results of operations could still be materially and adversely affected if these security breaches result in the affected television network operators having difficulty recruiting new subscribers or retaining existing subscribers. Furthermore, as our CA systems are used on the affected networks, our reputation could also be severely harmed by being associated with such security breaches on our customers' networks.

***We generally do not have long-term contracts with suppliers of computer chips or the companies that manufacture our smart cards. If any of our computer chip suppliers or smart-card manufacturers is unable to fulfill our orders in time or at all, we may be unable to deliver smart cards to our customers, which could severely damage our business, profitability and prospects.***

As a general matter, we do not have long-term contracts with our suppliers. We purchase substantially all of the computer chips that are used in our smart cards from two suppliers, STMicroelectronics, or STM, and Infineon Technologies AG, or Infineon (and prior to February 2009, indirectly through an agent of Infineon). In addition, we have arrangements with a number of smart-card manufacturers, including China Electronics Smart Card Co., Ltd., or China Electronics, the China Sciences Group and Axalto Smart Card Technology Co., to embed the computer chips into plastic cards. We generally place purchase orders with our computer chip and smart card suppliers as needed to meet our customers' demand. Our computer chip and smart card suppliers are generally not under any contractual obligation to accept our purchase orders or fulfill them within our desired time frame. However, we currently maintain a one-year contract with each of China Electronics and the China Sciences Group that requires them to fulfill our orders in accordance with an agreed schedule. Any significant delay or failure by any of our suppliers or manufacturers to fulfill our orders for computer chips or smart cards could force us to obtain computer chips or smart cards from alternative sources at higher cost, negatively affecting our operating margins, or could prevent us from delivering smart cards in the required quantities to our customers on time. Any such failure by us could have a material adverse effect on our reputation and ability to retain customers, as well as our business, financial condition and results of operations, and may also subject us to claims from our customers.

***We face intense competition, which could reduce our market share and harm our financial performance.***

**Table of Contents**

The market for digital television CA systems and software applications is intensely competitive. Several of the world's leading developers and producers of CA systems, including Irdeto Access B.V., Conax Company and Kudelski SA, operate in the PRC market. We also compete with domestic CA systems vendors, including Sumavision Technologies Co., Ltd. and DVN Holdings Ltd. Some of our competitors have substantially greater financial, technical and other resources than we do, and may respond more quickly than we could to technological or commercial changes in our industry. In addition, some competitors offer their CA systems at a lower price or with a longer credit term than we do. We may need to reduce our prices to compete with them, which may lead to reduced margins or loss of market share. We cannot assure you that we will be able to compete effectively in the market for digital television CA systems and software applications in the PRC. See Item 4. Information on the Company B. Business Overview Competition.

***We depend upon key personnel, including our senior executives and technical and engineering staff, and our business and prospects would greatly suffer if we lose their services.***

Our future success depends heavily on the continued service of our key executives. In particular, we rely on the expertise and experience of Jianhua Zhu, chairman of our board of directors and our chief executive officer, Dr. Zengxiang Lu, member of our board of directors, and Dong Li, our president and chief marketing officer, in our business operations and technology development efforts, and on their relationships with the regulatory authorities, our customers, our suppliers, our employees and our operating company, N-S Digital TV. If any of them becomes unable or unwilling to continue in their present positions, or if they join a competitor or form a competing company, we may not be able to replace them easily, our business may be significantly disrupted and our business, financial condition and results of operations may be materially and adversely affected. We do not currently maintain key-man insurance for any of our key personnel. Furthermore, our future success depends heavily upon our ability to recruit and retain experienced technical and engineering staff. There is substantial competition for qualified technical personnel from other companies in our industry as well as from businesses outside our industry, and we may not be successful in retaining technical and engineering employees and recruiting new ones. If we are unsuccessful in our recruitment and retention efforts, our business and prospects may be materially and adversely affected.

***Our attempts to diversify our business and expand our revenues by providing new solutions and products may not be successful and may prove costly.***

We have been pursuing strategies to expand and diversify our revenues, including developing and commercializing new solutions and products, such as value-added digital television services, cloud computing technology-based digital video delivery solutions and advanced digital television terminals. To this end, we established Beijing Novel-Super Media Investment Co., Ltd., or N-S Media Investment, Beijing Cyber Cloud Co., Ltd., or Cyber Cloud, Beijing Joysee Technology Co., Ltd., or Joysee, and Beijing Super Movie Technology Co., Ltd., or Super Movie, during the past years. See Item 4. Information on the Company A. History and Development of the Company. However, we have no prior experience cooperating with television network operators or other third parties in providing new solutions and products, and may not be successful in doing so. In addition, our attempts to develop this new business model may be time-consuming and may distract our management from developing our existing lines of business, which could have a material adverse effect on our business, financial condition and results of operations.

***We may face difficulties implementing our acquisition strategy, including identifying suitable opportunities and integrating acquired businesses and assets with our existing operations.***

As part of our business strategy, we intend to enhance our capabilities by acquiring other companies, businesses or technologies that complement our existing business or enhance our product portfolio and proprietary technology. However, our ability to implement our acquisition strategy will depend on our ability to identify suitable acquisition candidates, our ability to compete effectively to attract and reach agreement with acquisition candidates on commercially reasonable terms and the availability of financing to complete larger acquisitions, as well as our ability to obtain any required shareholder or government approvals. In addition, any particular acquisition may not produce the intended benefits. For example, we may not be successful in integrating acquisitions with our existing operations and personnel, and the process of integration may cause unforeseen operating difficulties and expenditures and may attract significant attention of our management that would otherwise be available for the ongoing development of our business. If we make future acquisitions, we may issue new shares that dilute the interests of our other shareholders, expend cash, incur debt, assume contingent liabilities or create additional expenses related to the impairment of goodwill or the amortization of other intangible assets with estimable useful lives.

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**Table of Contents**

*Our business could be harmed if a defect in our software, technology or services interferes with, or causes any failure in, our customers systems.*

Our software and technology are integrated into the television transmission infrastructure of our customers. Accordingly, a defect, error or performance problem with our software or technology could interfere with, or cause a critical component of, one or more of our customers systems to fail for a period of time. Any negligence or error of our employees in the course of their performance of system integration, upgrade or maintenance services for our customers may also cause malfunctioning, suspension or failure of our customers systems. Occurrence of such incidents could result in claims for substantial damages against us, regardless of whether we are responsible for such failure. Any claim brought against us could be expensive to defend and require the expenditure of a significant amount of resources, regardless of whether we prevail. In addition, we do not currently maintain any product or business liability insurance. Although we have not experienced any such material interference or failure in the past, our potential exposure to this risk may increase as sales of our products and customer demand for our upgrade or maintenance services grow. Any future problem in this area could cause severe customer service and public relations problems for our customers.

*N-S Digital TV may be deemed not to be in full compliance with certain legal regulatory requirements relating to the production, sale and export of encryption products, and the relevant PRC government authorities could require N-S Digital TV to cease such activities and impose administrative penalties including fines, which could have a material adverse effect on our business, financial condition and results of operations.*

The PRC government introduced regulations in 1999 generally requiring a company that engages in the production and sale of encryption products to obtain two licenses, one for the production of encryption products and the other for the sale and distribution of encryption products, and the implementation rules for issuing these two licenses were promulgated in December 2005. Under these regulations and implementation rules, a company generally is only allowed to produce and/or sell encryption products that use algorithms designated by the encryption authority and such products shall also be certified by the encryption authority. In addition, these regulations and implementation rules also require a company obtain prior approval from the encryption authority for the export of encryption products. The encryption authority initially designated permitted algorithms for CA systems in 2007 and a final and official designation remains pending. Like many other vendors of CA systems in the PRC, N-S Digital TV has been producing and selling CA systems using algorithms other than those initially designated by the encryption authority. We understand that, in practice, the PRC government has allowed a transition period, of a duration yet to be determined at its sole discretion, for vendors of CA systems to comply with this requirement to use the algorithms to be finally and officially designated by the government. See Item 4. Information on the Company B. Business Overview Regulation Regulation of Encryption Industry. N-S Digital TV has engaged in the production and sale of encryption products since its establishment in May 2004, but it did not obtain the license for the production of encryption products until June 2006 and the license for the sale of encryption products until September 2008. In December 2008 and February 2009, certain CA system products we developed by using the algorithms designated by the encryption authority were certified by the encryption authority. However, we have not decided when N-S Digital TV will produce and sell those products using the designated algorithms, and various factors, in addition to the permissible transition period for adoption, will affect this decision, including whether products using algorithms designated by the encryption authority will be generally accepted by the cable television industry (including CA system vendors and cable television operators). Furthermore, N-S Digital TV has engaged in the export of encryption products since 2010, but it did not obtain the prior approval from the encryption authority for such export. If N-S Digital TV fails to adopt the algorithms designated by the encryption authority for any of CA systems products it produces and sells by the end of the transition period or at any time during the transition period at the request of the government, it may be required to discontinue the production and sale of its non-compliant CA systems. If the relevant PRC government authorities deem N-S Digital TV's production of encryption products prior to June 2006, sale of encryption products prior to September 2008 or export of encryption products since 2010 to be in violation of the applicable regulations, they may impose sanctions against N-S Digital TV. These sanctions may include confiscation of income from non-compliant activities, fines of up to three times the amount of income from non-compliant activities and revocation of the licenses already issued. Imposition of such sanctions may result in material disruptions to our business operations, damage to our reputation and significant financial losses.

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**Table of Contents**

***Enforcement of certain PRC regulatory requirements regarding the use of encryption products may prevent prospective customers from purchasing our CA systems and our business revenues and net income could be materially reduced as a result.***

The PRC government introduced regulations in 1999 that require users to use only encryption products that are certified by the encryption authority. The CA systems we currently produce and sell have not been certified by the encryption authority because we have not adopted the government-designated algorithms for such CA systems. We believe that because the PRC government provides for a transition period, which will be for a duration to be determined at its sole discretion, for us to adopt the algorithms to be finally and officially designated by the government, it is unlikely that the government will enforce the above-mentioned regulatory requirements with respect to the use or purchase of our CA systems during that transition period. In December 2008 and February 2009, certain CA system products we developed by using the algorithms designated by the encryption authority were certified by the encryption authority. However, as stated above, we have not decided when N-S Digital TV will produce and sell those CA system products certified by the encryption authority and various factors, in addition to the permissible transition period for adoption, will affect this decision. If we have not obtained the certification for the CA systems that we produce and sell upon the expiration of the transition period or at an earlier time the PRC government may otherwise require, enforcement of the above-mentioned regulatory requirements could prevent our prospective customers from purchasing our non-compliant CA systems, which could materially reduce our revenues and net income. In addition, even if we produce and sell products certified by the PRC encryption authority, we cannot assure you that we will be able to successfully market and sell such products.

***We may incur development costs and may be required to pay certain fees in order to use the algorithms designated by the PRC encryption authority for CA systems.***

A company generally is only allowed to produce and/or sell encryption products that have adopted the algorithms designated by the PRC encryption authority. As the encryption authority did not designate any algorithms for CA systems until 2007, we have been using algorithms in our CA systems other than those designated by the encryption authority. If we are required by the government authorities to instead use the algorithms designated by the encryption authority in our CA systems, we may incur costs to develop new products adopting such algorithms and may have to pay certain fees to the government for such usage. Development costs and the payment of such fees, the amount of which remains unclear, may cause our profit margin to decline significantly as well as materially reduce our profitability.

***If we fail to protect our intellectual property rights, it could harm our business and competitive position.***

We are required to continually improve our products and services to stay competitive in the marketplace, and as a result intellectual property is critical to our continued success. We rely on a combination of patent, trademark and copyright laws, trade secrets, confidentiality procedures and contractual provisions to protect our intellectual property rights and the obligations we have to third parties from whom we license intellectual property rights. Nevertheless, these afford only limited protection and policing unauthorized use of proprietary technology can be difficult and expensive. In addition, intellectual property rights historically have not been enforced in the PRC to the same extent as in the United States, and intellectual property theft presents a serious risk in doing business in the PRC. We may not be able to detect unauthorized use of, or take appropriate steps to enforce, our intellectual property rights and this could have a material adverse effect on our business, financial condition and results of operations.

***We may be exposed to infringement or misappropriation claims by third parties that, if determined adversely to us, could require us to pay significant damage awards.***

Our success depends largely on our ability to use and develop our technology and know-how without infringing the intellectual property rights of third parties. The validity and scope of any claims relating to our technology patents would involve complex technological, legal and factual questions and analyses and, as a result, the outcome would be highly uncertain. We may be subject to litigation involving claims of patent infringement or violation of other intellectual property rights of third parties. The defense of such claims would be both costly and time-consuming, and could significantly divert the efforts and resources of our management and technical personnel. An adverse determination in any such litigation or proceedings to which we may become a party could subject us to significant liability to third parties, require us to seek licenses from third parties, pay ongoing royalties or redesign our products, or subject us to injunctions prohibiting the manufacture and sale of our products or the use of our technologies. Protracted litigation could also result in our customers or potential customers deferring or limiting their purchase or use of our products until resolution of such litigation. In addition, we could face disruptions to our business and damage to our reputation, and our financial condition and results of operations could be materially adversely affected.

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**Table of Contents**

***We rely on a single facility for most of our business operations. Any destruction of, or significant disruption to, this facility could severely affect our ability to conduct normal business operations.***

Most of our business operations, including the encoding of our smart cards, which is an essential part of the smart card manufacturing process, all our research and development activities and our corporate headquarters are concentrated within a single facility that we lease in Beijing, PRC. As we do not maintain back-up facilities, we rely on this facility for the continued operation of our business. In addition, we currently do not maintain any business disruption or similar insurance coverage. A major earthquake, fire or other catastrophic event that results in the destruction of, or significant disruption to, the facility could severely affect our ability to complete sales or conduct other normal business operations, which would materially reduce our revenues and net income.

***Our operating results may fluctuate significantly from quarter to quarter, which could adversely affect the price of our ADSs.***

Our quarterly operating results have varied significantly in the past and are likely to continue to vary significantly in the future. Our quarterly revenues may fluctuate as a result of a number of factors, many of which are outside of our control. For example, our quarterly revenues substantially depend upon the timing of smart card orders placed by our customers. A significant portion of our quarterly revenues has generally reflected orders from a small number of large customers for our CA systems. Our cost of revenues and operating expenses may also fluctuate from quarter to quarter. As a result, you may not be able to rely on period-to-period comparisons of our operating results as an indication of our future performance. In addition, our actual quarterly results may differ from market expectations, which may cause the price of our ADSs to decline significantly.

***Failure to manage our growth or develop appropriate internal organizational structures, internal control environment and risk monitoring and management systems in line with our growth could have a material adverse effect on our business and prospects.***

Our business and operations have expanded since our formation in 2004. Significant management resources must be expended to develop and implement appropriate structures for internal organization and information flow, an effective internal control environment and risk monitoring and management systems in line with our growth, as well as to hire and integrate qualified employees into our organization. We cannot assure you that our existing internal control and risk monitoring and management systems would continue to be adequate. If we fail to appropriately develop and implement structures for internal organization and information flow, an effective internal control environment and a risk monitoring and management system, we may not be able to identify unfavorable business trends, administrative oversights or other risks that could materially and adversely affect our business, financial condition and results of operations.

***If we fail to maintain an effective system of internal control over financial reporting, our ability to accurately and timely report our financial results or prevent fraud would suffer. As a result, investor confidence and the trading price of our ADSs may be materially and adversely impacted.***

We are subject to the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act. Section 404 of the Sarbanes-Oxley Act requires that we include a report of management on our internal control over financial reporting in our annual report on Form 20-F. In addition, our independent registered public accounting firm must report on the effectiveness of our internal control over financial reporting. Our management concluded that our internal control over financial reporting was effective as of December 31, 2012, the end of the period covered by this annual report, and our independent registered public accounting firm opined that we maintained effective internal control over financial reporting of the same period. However, we may fail to maintain effective internal control over financial reporting in the future, in which case we and the independent registered public accounting firm may not be able to conclude that we have effective internal control over financial reporting. Moreover, even if our management concludes that our internal control over financial reporting is effective, our independent registered public accounting firm, or the relevant regulators, may disagree. If such independent registered public accounting firm is not satisfied with our internal control or the level at which our control is documented, designed, operated or reviewed, or if it interprets the relevant requirements differently from us, then it may not be able to issue an unqualified opinion. In addition, our reporting obligations as a public company may place a significant strain on our management, operational and financial resources and systems for the foreseeable future.

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**Table of Contents**

Moreover, if we fail to maintain the adequacy of our internal control over financial reporting, as these standards are modified, supplemented or amended from time to time, we may not be able to conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act. If we fail to achieve and maintain an effective internal control environment, we could suffer material misstatements in our financial statements and fail to meet our reporting obligations, which would likely cause investors to lose confidence in our reported financial information. This could harm our operating results and lead to a significant decline in the trading price of our ADSs. Furthermore, ineffective internal control over financial reporting could expose us to increased risk of fraud or misuse of corporate assets and subject us to potential delisting from the stock exchange on which we list, regulatory investigations and civil or criminal sanctions.

*We may need additional capital and we may not be able to obtain it.*

In order for us to grow, remain competitive, develop new products and services, expand our customer base and carry out acquisitions, we may seek to obtain additional capital in the future through selling additional equity or debt securities or obtaining a credit facility. Our ability to obtain additional capital in the future is subject to a variety of uncertainties, including:

our future financial condition, results of operations and cash flows;

conditions in the United States and other capital markets in which we may seek to raise funds;

investors' perception of, and demand for, securities of digital television components and related companies; and

economic, political and other conditions in the PRC and elsewhere.

We may be unable to obtain additional capital in a timely manner or on acceptable terms or at all. Furthermore, the additional issuances of equity securities may result in significant dilution to our shareholders. The incurrence of debt would result in increased interest expense and could require us to agree to operating and financial covenants that would restrict our operations.

*We were classified as a passive foreign investment company, or PFIC, for each year of 2009 through 2012, which resulted in adverse United States federal income tax consequences to U.S. holders of our ADSs and may result in additional adverse United States Federal income tax consequences to such holders in subsequent years.*

Based on analyses of the value of our assets as of December 31, 2012 and the ends of earlier years, we were a PFIC during the taxable years 2009 through 2012 for U.S. federal income tax purposes. We have substantial passive assets in the form of cash and cash equivalents, among others, and can provide no assurance that we will not continue to be classified as a PFIC for the taxable year 2013 or future taxable years, as PFIC status is tested each year and depends on our assets and income in such year. Our PFIC status for the current taxable year 2013 will not be determinable until the close of the taxable year ending December 31, 2013.

We will be classified as a PFIC in any future taxable year if either: (1) the average percentage value of our gross assets during the taxable year that produce passive income or are held for the production of passive income is at least 50% of the value of our total gross assets; or (2) 75% or more of our gross income for the taxable year is passive income. If we hold substantial cash, cash equivalents and other passive assets, as we currently do, a significant decrease in the market price of our outstanding shares would increase the risk of us becoming a PFIC.

**Table of Contents**

In any taxable year in which we are classified as a PFIC, and you are a U.S. holder of our ADSs or shares, unless you make a mark-to-market election, you will generally be taxed at higher ordinary income rates, rather than lower capital gain rates, if you dispose of our ADSs or shares for a gain, even if we are not a PFIC in the year of disposition. In addition, a portion of the tax imposed on your gain would be increased by an interest charge if you dispose of our ADSs or shares in a year later than the first year in which we were treated as a PFIC that you hold our ADSs or shares. Similar treatment would apply if you receive distributions from us that are characterized as excess distributions. Moreover, you will not be able to benefit from any preferential tax rate with respect to any dividend distribution that you may receive from us in a year in which we are a PFIC or in the following year. Finally, you will also be subject to special United States federal income tax reporting requirements. For more information on the United States federal income tax consequences to you that would result from our classification as a PFIC, including the consequences of making a mark to market selection, see Item 10. Additional Information E. Taxation United States Federal Income Taxation PFIC Rules. You should consult your tax advisor regarding the application of the PFIC rules to your investment in our ADSs or shares.

***Our bank accounts are not insured or similarly protected against loss.***

As of December 31, 2012, approximately 96.7% of our bank deposits were placed with two commercial banks in the PRC. Unlike certain other jurisdictions, applicable PRC laws do not require that banks provide deposit insurance or similar protections to depositors in the PRC. As a result, our bank accounts are not insured or similarly protected. If a commercial bank with which we have placed our cash deposits becomes insolvent, or if we are otherwise unable to withdraw funds, we may be unable to recover the cash on deposit with that bank. As a result, our liquidity and cash flows, as well as financial condition and results of operations, could be materially and adversely affected.

**Risks Relating to Our Corporate Structure**

***If the PRC government determines that N-S Digital TV is a vendor of non-PRC CA systems by virtue of the agreements that establish the structure for operating our business, we could face difficulty selling our CA systems in the PRC.***

SARFT policy requires any cable television network operator who uses a non-PRC CA system to install a parallel PRC CA system. Under this policy, vendors of non-PRC CA systems may sell only to cable network operators who have already installed a PRC CA system or who are willing to purchase a parallel PRC CA system. This may result in a competitive disadvantage for vendors of non-PRC CA systems relative to vendors of PRC CA systems. Such policy does not expressly indicate whether the CA systems produced by a foreign-invested company incorporated in the PRC, such as our subsidiary Beijing Super TV Co., Ltd., or Super TV, fall into the category of non-PRC CA systems. In light of this ambiguity, in order to avoid our CA systems being deemed non-PRC CA systems, we have established N-S Digital TV, which is wholly owned by PRC persons, to produce and sell our CA systems. We do not have any equity interest in N-S Digital TV and instead enjoy the economic benefits of, and have substantive control over, N-S Digital TV through contractual arrangements with N-S Digital TV and its shareholders. N-S Digital TV also holds the licenses and approvals that are essential to our business, and we derive a significant portion of our revenues from N-S Digital TV.

There are substantial uncertainties regarding the interpretation and application of the above-described PRC government policy and relevant PRC laws and regulations. Accordingly, the PRC government may determine that N-S Digital TV is a vendor of non-PRC CA systems by virtue of our contractual arrangements with N-S Digital TV and its shareholders. If N-S Digital TV is deemed to be a vendor of non-PRC CA systems by the PRC government, cable network operators may cancel their orders for our CA systems to avoid being required to install a parallel PRC CA system, and we may also lose potential customers who are not willing, or have no plan, to install a parallel PRC CA system for economic or other reasons. As a result, our business, financial condition and results of operations could be materially and adversely affected.

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**Table of Contents**

*The agreements that establish the structure for operating our business may result in the relevant PRC government regulators revoking or refusing to renew N-S Digital TV's licenses for the production and sale of commercial encryption products, or refusing to issue any other license required to engage in an encryption-related business.*

Our CA systems business uses encryption technology and thus is required by the relevant PRC laws, rules and regulations to obtain licenses to produce and sell commercial encryption products. Although foreign-invested enterprises incorporated in the PRC, such as our subsidiary, Super TV, are not expressly prohibited from conducting a business that uses encryption technology, foreign-invested enterprises may have difficulty obtaining the necessary license due to the PRC encryption authority's generally restrictive approach towards foreign participation in the PRC encryption industry. N-S Digital TV, which is wholly owned by PRC persons and through which we conduct our CA systems business, has obtained licenses to produce and sell commercial encryption products as required for our business.

Our contractual arrangements with N-S Digital TV and its shareholders provide us with the economic benefits of, and substantive control over, N-S Digital TV. If the PRC encryption authority determines that our control over, or relationship with, N-S Digital TV through those contractual arrangements is contrary to their generally restrictive approach towards foreign participation in the PRC encryption industry, we cannot assure you that the PRC encryption authority will not reconsider N-S Digital TV's eligibility to hold the licenses to produce and sell commercial encryption products. The PRC encryption authority may revoke, or refuse to renew, N-S Digital TV's licenses to produce and sell commercial encryption products, or refuse to grant any other encryption-related license that may be required for our business in the future. If that were to happen, we might have to discontinue all or a substantial portion of our business pending the reissuance, extension or issuance of the required license. In addition, we might have to restructure our operation in order to have such licenses reissued, extended or issued. Such restructuring may result in a loss or reduction of our control over, or the economic benefits we enjoy from, N-S Digital TV under existing contractual arrangements. As a result, our business, financial condition and results of operations could be materially and adversely affected.

*Our business and operations could be significantly disrupted, and we could be subject to sanctions, if the contractual arrangements between us and our consolidated variable interest entity, N-S Digital TV, which we depend on for the production and sales of our CA systems, are found to be in violation of applicable PRC laws, rules and regulations.*

We conduct substantially all of our CA systems business through N-S Digital TV, a PRC company that we control through contractual arrangements. For a description of such contractual arrangements, see Item 7. Major Shareholders and Related Party Transactions - B. Related Party Transactions. As PRC laws, rules and regulations are evolving and subject to differing interpretations, there exist substantial uncertainties regarding the validity and enforceability of the contractual arrangements between us and N-S Digital TV and its shareholders. We have been advised by our PRC legal counsel, Han Kun, that the ownership structures of our operating subsidiary in China and our consolidated variable interest entity comply with existing PRC laws, rules and regulations. Moreover, Han Kun is of the opinion that each of the agreements that establish the contractual arrangements is valid, legally binding and enforceable and does not violate applicable PRC laws, rules and regulations.

We cannot assure you that the relevant PRC regulatory authorities will not ultimately determine that these contractual arrangements do not comply with applicable PRC laws, rules and regulations. In addition, in late 2011, various media sources reported that the research division of the China Securities Regulatory Commission, or the CSRC, had prepared a report for the State Council of the PRC proposing to regulate the use of the variable interest entity structure, such as the structure used by us, in the context of foreign investment in the PRC and overseas listings of PRC companies. It is unclear, however, whether the CSRC has officially submitted such a report to the State Council, what specific content such report contains and whether and when any further action will be taken by the State Council, the CSRC, the Ministry of Commerce, or the MOFCOM, or any other PRC government authority regarding the use of the variable interest entity structure.

If we or our operating company were found to be in violation of PRC laws, rules or regulations, the relevant PRC regulatory authorities would have broad discretion in imposing sanctions, including, without limitation:

**Table of Contents**

levying fines;

confiscating income;

revoking business licenses or operating licenses;

requiring us to revise our ownership structure or restructure our operations;

requiring the discontinuation of businesses;

restricting or requiring us to discontinue related party transactions among our PRC subsidiaries, on the one hand, and N-S Digital TV and its subsidiaries, on the other hand;

limiting our business expansion in China; and/or

imposing additional conditions or requirements with which we may not be able to comply.

Any of these or similar actions could cause significant disruptions to our business, as well as materially reduce our revenues, profitability and cash flows. In addition, if the imposition of any of these or similar sanctions causes us to lose the power to effectively control N-S Digital TV and its subsidiaries or the ability to receive substantially all the economic benefits of these entities, we may not be able to consolidate the financial results of N-S Digital TV and its subsidiaries into our financial statements under U.S. GAAP.

***Our contractual arrangements with our operating company, N-S Digital TV, and its shareholders may not be as effective in providing operational control as direct ownership and may be difficult to enforce.***

In order for our CA systems not to be deemed by the PRC government as non-PRC CA systems, which may result in a competitive disadvantage for us in the PRC market, we have established N-S Digital TV, which is wholly owned by PRC persons, to produce and sell our CA systems in the PRC. As a result, we generate a significant portion of our revenues through N-S Digital TV. We do not have any equity interest in N-S Digital TV and instead enjoy the economic benefits of, and have substantive control over, N-S Digital TV through contractual arrangements with N-S Digital TV and its shareholders. N-S Digital TV also holds the licenses and approvals that are essential to our business. For a description of such contractual arrangements, see Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions. These arrangements may not be as effective in providing control over our operations as direct ownership would be. In particular, N-S Digital TV could fail to perform or make payments as required under these contractual arrangements, and we would have to rely on the PRC legal system to enforce these arrangements, which may not be effective. See Risks Relating to the People's Republic of China Uncertainties in the interpretation and enforcement of PRC laws, rules and regulations could limit the legal protections available to you and us. If we are unable to enforce these contractual arrangements, or if we suffer significant delay or other obstacles in the process of enforcing these arrangements, our business and operations could be severely disrupted, which could materially and adversely affect our financial condition and results of operations as well as damage our reputation, and we may not be able to consolidate the financial results of N-S Digital TV and its subsidiaries into our financial statements in accordance with U.S. GAAP.

***The shareholders or directors of N-S Digital TV may have conflicts of interest with us.***

We do not have any equity interest in N-S Digital TV and instead enjoy the economic benefits of, and have substantive control over, N-S Digital TV through contractual arrangements with N-S Digital TV and its shareholders. Conflicts of interests may arise between us and the shareholders of N-S Digital TV, who are currently our employees and some of whom are currently our shareholders. In addition, two directors of N-S Digital TV are also directors of our company, and conflicts may arise between the duties they owe to N-S Digital TV and the duties they owe to us. We cannot assure you that if any such conflicts arise, any or all of the shareholders or directors of N-S Digital TV, as the case may be, will act in the best interests of our company or that such conflicts will be resolved in our favor. We have no specific policies or procedures for resolving any

such conflicts that may arise. In addition, these shareholders or directors may breach, or cause N-S Digital TV to breach or refuse to renew, the existing contractual arrangements that allow us to effectively control N-S Digital TV and receive economic benefits from it. If we cannot satisfactorily resolve any conflicts of interest or disputes between us and the shareholders or directors of N-S Digital TV, we may have to resort to legal proceedings, which may involve substantial uncertainty and result in disruptions to our business and operations.

## **Table of Contents**

***Contractual arrangements we have entered into between Super TV and N-S Digital TV may be subject to scrutiny by the PRC tax authorities and any finding that we or N-S Digital TV owe additional taxes could substantially reduce our net income and the value of your investment.***

Under applicable PRC laws, rules and regulations, arrangements and transactions among related parties may be subject to audit or challenge by the PRC tax authorities. We could face material adverse tax consequences if the PRC tax authorities determine that the contractual arrangements between Super TV, our wholly-owned subsidiary in the PRC, and N-S Digital TV do not represent an arm's-length price and consequently adjust N-S Digital TV's income in the form of a transfer pricing adjustment. A transfer pricing adjustment could, among other things, result in a reduction of expense deductions recorded by N-S Digital TV, which could in turn increase its tax liabilities. In addition, the PRC tax authorities may impose late payment fees and other penalties.

***Certain of our existing shareholders have substantial influence over our company and their interests may not be aligned with the interests of our other shareholders.***

As of March 31, 2013, our three largest shareholders beneficially owned a total of approximately 47.8% of our outstanding shares. Accordingly, they will have significant influence in determining the outcome of any corporate transaction or other matter submitted to the shareholders for approval, including mergers, consolidations and the sale of all or substantially all of our assets, election of directors and other significant corporate actions. They will also have the power to prevent or cause a change in control. In addition, without the consent of these shareholders, we could be prevented from entering into transactions that could be beneficial to us. These shareholders may cause us to take actions that are opposed by other shareholders as the interests of these shareholders may differ from the interests of our other shareholders. See Item 7. Major Shareholders and Related Party Transactions for more information regarding the share ownership of our officers, directors and significant shareholders.

## **Risks Relating to the People's Republic of China**

***Our operations may be materially adversely affected by changes in the economic, political and social conditions of the PRC.***

Substantially all of our non-cash assets are located in, and substantially all of our revenue is sourced from, the PRC. Accordingly, our business, financial condition, results of operations and prospects may be influenced to a significant degree by political, economic and social conditions in the PRC generally and by continued economic growth in the PRC as a whole.

The PRC economy differs from the economies of most developed countries in many respects, including with respect to the extent of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth over the past three decades, growth has been uneven across different regions and among various economic sectors. The PRC government has implemented various measures to encourage economic development and guide the allocation of resources. Some of these measures benefit the overall PRC economy, but may also have a negative effect on us. For example, our operating results and financial condition may be adversely affected by government control over capital investments or changes in tax regulations that are applicable to us. We cannot predict the possible impact of any future economic policies of the PRC government on our business and operations.

The PRC government has implemented various measures since 2011 to control inflation, such as tightening bank lending policies and increasing interest rates. In addition, China's 2012 annual gross domestic product growth rate was 7.8%, the slowest since 1999 and down from 9.3% in 2011. Continued implementation of these or similar measures, or a variety of other factors, may cause a continued slowdown in the PRC economy, which, in turn, could significantly reduce business activities in the PRC, including a slowing-down or decline in investment in cable television networks, which in turn may result in a reduction of demand for our products and services and thus materially reduce our revenues and profitability.

**Table of Contents**

***Uncertainties in the interpretation and enforcement of PRC laws, rules and regulations could limit the legal protections available to you and us.***

The PRC legal system is a civil law system based on written statutes. Unlike common law systems, it is a system in which legal decisions have limited value as precedents. In 1979, the PRC government began to promulgate a comprehensive system of laws and regulations governing economic matters in general. The overall effect of legislation over the past three decades has significantly increased the protections afforded to various forms of foreign or private-sector investment in the PRC. Our PRC operating subsidiary, Super TV, is a foreign-invested enterprise and is subject to laws, rules and regulations applicable to foreign investment in the PRC as well as laws and regulations applicable to foreign-invested enterprises. N-S Digital TV is a privately owned company and is subject to various PRC laws, rules and regulations that are generally applicable to companies in the PRC. These laws, rules and regulations change frequently, and their interpretation and enforcement involve uncertainties. For example, we may have to resort to administrative and court proceedings to enforce the legal protections that we enjoy either by law or contract. However, since PRC administrative and court authorities have significant discretion in interpreting and implementing statutory and contractual terms, it may be more difficult to evaluate the outcome of administrative and court proceedings and the level of legal protection we enjoy than in more developed legal systems. These uncertainties may also impede our ability to enforce the contracts we have entered into, and materially impair our business and operations.

***The approval of the CSRC might be required in connection with our initial public offering under certain PRC regulation; failure to obtain this approval, if required, could have a material adverse effect on our business, financial condition, results of operations and reputation as well as the trading price of our ADSs.***

On August 8, 2006, six PRC regulatory agencies, including the MOFCOM, the State-owned Assets Supervision and Administration Commission, the State Administration for Taxation, or the SAT, the State Administration for Industry and Commerce, the CSRC and the State Administration of Foreign Exchange, or the SAFE, jointly adopted the *Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors*, or the M&A Rules, which became effective on September 8, 2006 and was amended on June 22, 2009. The M&A Rules, among other things, include provisions that purport to require that an offshore special purpose vehicle formed for the purpose of an overseas listing of securities in a PRC company obtain the approval of the CSRC prior to the listing and trading of such special purpose vehicle's securities on an overseas stock exchange.

We completed the initial listing and trading of our ADSs on the New York Stock Exchange, or the NYSE, on October 11, 2007. We did not seek CSRC approval in connection with our initial public offering. Our PRC counsel, Han Kun, advised us that, based on their understanding of the current PRC laws, regulations and rules, because we completed our restructuring in 2004 in connection with an equity investment in our company by a private equity investor more than two years prior to the promulgation of the M&A Rules, we were not and are not required by the M&A Rules to apply to the CSRC for approval of our initial public offering, unless we are clearly required to do so by any rules promulgated in the future. See Item 4. Information on the Company B. Business Overview Regulation Regulation of Overseas Listings. However, the application of the M&A Rules remains unclear. If the CSRC or another PRC regulatory agency subsequently determines that the CSRC's approval was required for our initial public offering, we may face sanctions by the CSRC or another PRC regulatory agency. If this happens, these regulatory agencies may impose fines and penalties on our operations in the PRC, limit our privileges in the PRC, or take other actions that could have a material adverse effect on our business, financial condition, results of operations and prospects, as well as the trading price of our ADSs.

***PRC regulations relating to offshore investment activities by PRC residents may increase the administrative burden we face and create regulatory uncertainties that could restrict our overseas and cross-border investment activity, and a failure by our shareholders who are PRC residents to make any required applications and filings pursuant to such regulations may prevent us from being able to distribute profits and could expose us and our PRC resident shareholders to liability under PRC law.***

The SAFE has promulgated several regulations, including the *Notice on Issues Relating to the Administration of Foreign Exchange in Fund-Raising and Round-Trip Investment Activities of Domestic Residents via Offshore Special Purpose Companies*, or SAFE Notice 75, and its implementation rules and guidances, that require PRC residents and PRC corporate entities to register with and obtain approvals from relevant PRC government authorities in connection with their direct or indirect offshore investment activities. These regulations may apply to our shareholders who are PRC residents in connection with our prior and any future offshore acquisitions.

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**Table of Contents**

The SAFE regulations required registration by March 31, 2006 of direct or indirect investments previously made by PRC residents in offshore companies prior to the implementation of the SAFE Notice 75 on November 1, 2005. In addition, under the SAFE regulations, any PRC resident who is a direct or indirect shareholder of an offshore company is required to update his previously filed registration with respect to such offshore company to reflect any material change. If a PRC shareholder with a direct or indirect stake in an offshore parent company fails to make the required SAFE registration or update the previously filed registration, the PRC subsidiaries of such offshore parent company may be prohibited from making distributions of profit to the offshore parent and from paying the offshore parent proceeds from any reduction in capital, share transfer or liquidation in respect of the PRC subsidiaries. Furthermore, failure to comply with the various SAFE registration requirements described above could result in liability under PRC law for foreign exchange evasion.

We have notified holders of our ordinary shares whom we know are PRC residents to register with the local branches of the SAFE and update their registration as required by the relevant SAFE regulations described above. However, we cannot assure you that all of our shareholders who are PRC residents will comply with our request to make or obtain any registrations or approvals or update their previously filed registrations as required under these regulations or other related legislation. If any existing shareholder transfers any of our shares or ADSs to another PRC resident, it is unclear whether such new shareholder is also required to make the SAFE registration. Furthermore, as the interpretations and practice in implementing these SAFE regulations have been constantly evolving, it is unclear how these regulations, and any future regulation concerning offshore or cross-border transactions, will be interpreted, amended and implemented by the relevant government authorities. The failure or inability of our PRC resident shareholders to obtain any required approvals or make any required registrations may subject us to fines and legal sanctions, restrict our cross-border investment activities or obtaining of shareholders loans, and prevent us from being able to make distributions or pay dividends, as a result of which our business as well as our ability to distribute profits to you could be materially and adversely affected.

***We may be subject to fines and legal sanctions if we or our employees who are domestic individuals fail to comply with the PRC regulations relating to employee share options granted by overseas-listed companies to domestic individuals.***

In February 2012, the SAFE promulgated the Notice relating to Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas-Listed Companies, or SAFE Notice 7, which superseded the Application Procedures of Foreign Exchange Administration for Domestic Individuals Participating in Employee Stock Holding Plans or Stock Option Plans of Overseas-Listed Companies, or SAFE Notice 78, promulgated by the SAFE in March 2007. SAFE Notice 7 is applicable to directors, supervisors, senior management personnel and other employees of an overseas-listed company incorporated in the PRC, PRC subsidiaries or branches of an overseas-listed company, and any PRC entities which are directly or indirectly controlled by an overseas-listed company, or, collectively, Domestic Companies, including PRC citizens (including Hong Kong, Macau and Taiwan) and foreign citizens who have resided in the PRC for one year or longer, or, collectively, Domestic Individuals. Under SAFE Notice 7, Domestic Individuals who participate in a stock incentive plan of an overseas-listed company are required, through a Domestic Company or a PRC entity designated by a Domestic Company, or the Domestic Agent, to register with the SAFE or its authorized local counterparts and complete certain other procedures. As we are an overseas-listed company, we and our employees who are Domestic Individuals and have been granted share options or any other stock-related rights and benefits under our stock incentive plans are subject to SAFE Notice 7. We have registered for us and on behalf of our employees with the relevant local SAFE branch in 2008 for our 2005 Stock Incentive Plan pursuant to prior SAFE Notice 78, and we intend to register for us and on behalf of our employees who are Domestic Individuals for our 2008 Stock Incentive Plan, 2010 Stock Incentive Plan and 2012 Stock Incentive Plan pursuant to SAFE Notice 7. However, there exist significant uncertainties in practice with respect to the interpretation and implementation of SAFE Notice 7 and we cannot assure you that we or our employees who are Domestic Individuals will be in full compliance with SAFE Notice 7. If the SAFE or other PRC government authorities determine that we or our employees who are Domestic Individuals fail to comply with the provisions of SAFE Notice 7, we or they may be subject to fines and legal sanctions. See Item 4. Information on the Company B. Business Overview Regulation Stock Incentive Plans.

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## **Table of Contents**

***We may rely on dividends and other distributions on equity paid by our operating subsidiary to fund cash and financing requirements, and limitations on the ability of our operating subsidiary to pay dividends to us could materially restrict our ability to conduct our business.***

We, as a holding company, may rely on dividends and other distributions on equity paid by our operating subsidiary, Super TV, for our cash and financing requirements, including the funds necessary to pay dividends and other cash distributions to our shareholders, service any debt we may incur and pay our operating expenses. If Super TV incurs debt on its own behalf in the future, the instruments governing the debt may restrict its ability to pay dividends or make other distributions to us. Furthermore, relevant PRC laws, rules and regulations permit payments of dividends by Super TV only out of its retained earnings, if any, determined in accordance with PRC accounting standards and regulations.

Under applicable PRC laws, rules and regulations, Super TV is required to set aside 10% of its after-tax profits each year to fund a statutory reserve until the accumulated amount of such reserve has exceeded 50% of its registered capital. This reserve is not distributable as cash dividends to equity owners. As a result of these PRC laws, rules and regulations, Super TV is restricted in its ability to transfer a portion of its net assets to us in the form of dividends. Limitations on the ability of Super TV to pay dividends to us could materially and adversely limit our ability to grow, make investments or acquisitions that could be beneficial to our businesses, pay dividends, or otherwise fund and conduct our business.

***Restrictions on currency exchange may limit our ability to effectively utilize our revenues as well as the ability of our PRC subsidiaries to obtain debt or equity financing from financial institutions or investors outside the PRC, including us.***

Substantially all of our operating revenues have been denominated in Renminbi. The Renminbi is currently convertible under the current account, which includes dividends, trade and service-related foreign exchange transactions, but not under the capital account, which includes foreign direct investment and loans. Currently, Super TV may purchase foreign exchange for settlement of current account transactions, including purchase of imported computer chips and payment of dividends to us, without the approval of the SAFE by complying with certain procedural requirements. However, the relevant PRC governmental authorities may limit or eliminate our ability to purchase foreign currencies in the future for current account transactions. Since a significant amount of our future revenues will be denominated in Renminbi, any existing and future restrictions on currency exchange may limit our ability to utilize revenues generated in Renminbi to purchase computer chips from suppliers outside of the PRC or fund our business activities outside of the PRC denominated in foreign currencies or pay dividends in foreign currencies to our shareholders, including holders of our ADSs.

In addition, foreign exchange transactions under the capital account are still subject to limitations and require approvals from, or registration with, the SAFE and other relevant PRC governmental authorities. In particular, any loans to Super TV are subject to PRC regulations and approvals. For example:

loans by us to Super TV, a foreign-invested enterprise, cannot exceed statutory limits and must be registered with the SAFE or its local counterpart; and

loans by us to N-S Digital TV, which is a domestic PRC entity, and its subsidiaries must be approved by the relevant government authorities and must also be registered with the SAFE or its local counterpart.

This could affect the ability of Super TV to obtain foreign exchange through debt or equity financing, including by means of loans or capital contributions from us.

***Fluctuations in exchange rates could result in foreign currency exchange losses.***

As substantially all of our operating revenues are denominated in Renminbi and the net proceeds from our initial public offering are denominated in U.S. dollars, fluctuations in exchange rates between U.S. dollars and Renminbi will affect the relative purchasing power of these proceeds and our balance sheet and earnings per share in U.S. dollars. Appreciation or depreciation in the value of the Renminbi relative to the U.S. dollar would affect our financial results reported in U.S. dollar terms without giving effect to any underlying change in our business, financial condition or results of operations. Since July 2005, the Renminbi is no longer pegged solely to the U.S. dollar. Instead, the Renminbi is reported to be pegged against a basket of currencies, determined by the People's Bank of China, against which it can rise or fall by as much as 0.3% each day. This permitted floating range was raised to 0.5% in May 2007 and was further raised to 1% in April 2012. The Renminbi may appreciate or depreciate significantly in value against the U.S. dollar in the long term, depending on the fluctuation of the basket of currencies against which it is currently valued, or it may be permitted to enter into a full float, which may also result in a significant appreciation or depreciation of the Renminbi against the U.S. dollar. Fluctuations in the exchange rate will also affect the relative value of dividends, if any,

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payable on our ordinary shares in U.S. dollar terms and the value of any U.S. dollar-denominated investments we make in the future. In addition, since substantially all of our operating revenues are denominated in Renminbi while approximately 29.5% of our cost of revenues is denominated in U.S. dollars, fluctuations in the exchange rate could also impact our financial condition and results of operations.

## **Table of Contents**

Very limited hedging transactions are available in the PRC to reduce our exposure to exchange rate fluctuations. To date, we have not entered into any other hedging transactions. While we may decide to enter into hedging transactions in the future, the availability and effectiveness of hedging transactions may be limited and we may not be able to successfully hedge our exposure at all. In addition, our currency exchange losses may be magnified by PRC exchange control regulations that restrict our ability to convert Renminbi into foreign currency.

***The discontinuation of any of the preferential tax treatments or the financial incentives currently available to us in the PRC could materially and adversely affect our business, financial condition, results of operations and prospects.***

The PRC government has provided various incentives to Super TV and N-S Digital TV. These incentives include reduced enterprise income tax rates, value-added tax refunds and tax holidays. For example, as high-and-new technology enterprises, each of Super TV and N-S Digital TV was entitled to a preferential income tax rate of 15% (against the standard income tax rate of 25%) in each of 2010, 2011 and 2012. In addition, Super TV was designated as a key software enterprise for the tax years from 2010 to 2012 by the relevant PRC government authorities and, as a result, was entitled to a preferential income tax rate of 10% in each of those years. Furthermore, for certain software-related products that are qualified as software products by PRC tax authorities, we received tax refunds which effectively reduce the applicable value-added tax rate from 17% to 3%.

Super TV and N-S Digital TV must meet a number of financial and non-financial criteria in order to continue to qualify for the above tax incentives. For example, in order to be able to enjoy the preferential income tax rate of 15%, Super TV and N-S Digital TV must be qualified as high-and-new technology enterprises strongly supported by the State under the *PRC Enterprise Income Tax Law*, or the 2008 EIT Law, which took effect on January 1, 2008. In addition, in order to continue to enjoy the preferential income tax rate of 10%, Super TV must reapply for and obtain the designation as a key software enterprise biennially. Moreover, the PRC government could determine at any time to eliminate or reduce the scale of such preferential tax policies. See Item 5. Operating and Financial Review and Prospects A. Operating Results Taxes and Incentives PRC.

Any increase in Super TV's or N-S Digital TV's enterprise income tax rate or discontinuation or reduction of any of the preferential tax treatments or financial incentives currently enjoyed by Super TV or N-S Digital TV could have a material adverse effect on our business, financial condition, results of operations and prospects.

***We may be subject to PRC income tax on our global income, or dividends we receive from our PRC subsidiary may be subject to PRC withholding tax, depending on whether we are recognized as a resident enterprise in the PRC.***

Pursuant to the 2008 EIT Law and *Enterprise Income Tax Law Implementation Rules*, or the Implementation Rules, enacted by the State Council on December 6, 2007 and which became effective on January 1, 2008, an enterprise established under the laws of a foreign country or region whose de facto management body is located within the PRC territory is considered a resident enterprise and will generally be subject to the enterprise income tax at the rate of 25% on its global income as well as PRC enterprise income tax reporting obligations. According to the Implementation Rules, de facto management body refers to a managing body that exercises, in substance, overall management and control over the production and business, personnel, accounting and assets of an enterprise. The SAT issued the Notice on Issues Relating to Determination of Chinese-Controlled Offshore Enterprises as PRC Resident Enterprises by Applying the De Facto Management Body Test, or the SAT Notice 82, on April 22, 2009. The SAT Notice 82 provides for certain specific criteria for determining whether the de facto management body of a Chinese-controlled offshore enterprise is located in the PRC. In addition, on July 27, 2011, the SAT issued the *Administrative Measures of Enterprise Income Tax of Chinese-Controlled Offshore Resident Enterprises (Trial)*, or SAT Bulletin 45, which became effective on September 1, 2011, to provide guidance on the implementation of SAT Notice 82. SAT Bulletin 45 clarifies certain issues relating to: (i) the determination procedures of PRC resident enterprise status and (ii) tax registration and other related procedures for PRC resident enterprises. SAT Bulletin 45 also provides that if an offshore PRC resident enterprise presents a copy of the Chinese tax resident determination certificate issued by the competent tax authorities to a payer of PRC-sourced dividends, interest, royalties and other income, such payer shall not withhold income tax on these payments to the offshore PRC resident enterprise. Although each of the SAT Notice 82 and the SAT Bulletin 45 provides that it only applies to offshore enterprises controlled by PRC enterprises, not those controlled by PRC individuals, like our company, it is generally believed that the determining criteria set forth therein very likely reflect the SAT's general position as to how the de facto management body test should be applied to determine the tax residency of all offshore enterprises, regardless of whether they are controlled by PRC enterprises or individuals. With reference to the criteria set forth in the SAT Notice 82, we believe that we are not a PRC resident enterprise. However, if we were considered a PRC resident enterprise, although dividends we receive from our PRC operating subsidiary would be exempt from PRC withholding tax, we would be subject to the enterprise income tax at the rate of 25% on our global income as well as PRC enterprise income tax reporting obligations. In such case, our profitability and cash flow would be materially reduced as a result of our global income being taxed under the 2008 EIT Law.



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**Table of Contents**

If we are considered as a non-resident enterprise under the 2008 EIT Law, we will not be subject to the enterprise income tax at the rate of 25% on our global income. In such case, however, dividends we receive from our PRC subsidiary will be subject to a PRC withholding tax, the standard rate of which is 10% and can be reduced by an applicable tax treaty, under the 2008 EIT Law. According to the *Arrangement for Avoidance of Double Taxation on Income and Prevention of Tax Evasion* entered into between the PRC and Hong Kong in August 2006, as amended, dividends paid by a PRC foreign-invested enterprise to its shareholder in Hong Kong are generally subject to a 5% PRC withholding tax, subject to satisfaction of certain conditions and requirements, compared to the standard 10% PRC withholding tax under the 2008 EIT Law. However, on October 27, 2009, the SAT issued the *Notice on How to Recognize Beneficial Owners under Relevant Tax Treaties*, or the SAT Notice 601, which provides that only the enterprises with active operations can be recognized as beneficial owners under relevant tax treaties that are entitled to enjoy the corresponding tax benefits. The SAT Notice 601 further provides that those enterprises that are established solely for the purposes of benefiting from favorable tax treatment under the relevant tax treaties should not be recognized as beneficial owners and therefore cannot enjoy favorable tax treatment. On June 29, 2012, the SAT issued the *Announcement of the SAT Regarding Recognition of Beneficial Owners under Tax Treaties*, or the SAT Announcement 30, which provides that a comprehensive analysis based on all the factors listed in the SAT Notice 601 should be made to determine the beneficial owner status. We indirectly hold the 100% interest in our PRC subsidiary, Super TV, through Golden Benefit Technology Limited, or Golden Benefit, a wholly-owned subsidiary incorporated in Hong Kong. As a result, to the extent we are considered as a non-resident enterprise and Golden Benefit is not recognized as a qualified beneficial owner under the relevant tax treaty, dividends we receive from our PRC subsidiary will be subject to the standard rate of 10%. For example, we declared special cash dividends in November 2010 and 2012, respectively, and accordingly the 10% withholding tax was paid on the amount of distributable profits accumulated after January 1, 2008 of Super TV when it repatriated offshore for such dividend payments. In addition, as a result of our decision in 2012 to distribute the undistributed retained earnings of our PRC subsidiary without a set schedule, we accrued a US\$4.8 million deferred tax liability related to withholding tax on the undistributed earnings of Super TV generated after January 1, 2008. Such withholding tax increased our tax burden and reduced the amount of cash available to our company.

***Dividends payable by us to our non-PRC shareholders and ADS holders, and gains on the sales of our ordinary shares or ADSs, may be subject to withholding taxes under PRC tax laws, which may materially reduce the value of your investment.***

Prior to January 1, 2008, dividends payable to non-PRC enterprises were exempted from withholding tax. The 2008 EIT Law and the Implementation Rules, both of which became effective on January 1, 2008, provide that an income tax rate of 10% (which may be reduced by the relevant tax treaties between PRC and other jurisdictions) will generally be applicable to dividends payable to non-resident enterprises, which do not have an establishment or place of business in the PRC or whose establishment or place of business in the PRC has no connection with the dividends, to the extent such dividends are derived from sources within the PRC and paid out of distributable profits accumulated on or after January 1, 2008. In addition, any gain realized on the transfer of shares by non-resident enterprises is also subject to the 10% income tax if such gain is regarded as income derived from sources within the PRC, unless the applicable tax treaties provide for an alternative withholding arrangement. Furthermore, dividends payable to non-PRC individual investors and any gain realized on the transfer of our ADSs or ordinary shares by such non-PRC individual investors may be subject to PRC income tax at a rate of 20% (which may be reduced or exempted by the relevant tax treaties between PRC and other jurisdictions).

## **Table of Contents**

If we are considered as a PRC resident enterprise, our dividends payable to our non-PRC shareholders and ADS holders, and any gain realized from the transfer of our ordinary shares or ADSs, would be treated as income derived from sources within the PRC and would as a result be subject to PRC tax. If dividends payable to our non-PRC shareholders and ADS holders are subject to PRC tax, or if non-PRC shareholders and ADS holders are required to pay PRC tax on the transfer of our ordinary shares or ADSs, the value of your investment in our ordinary shares or ADSs may be materially reduced.

***The M&A Rules and other recent PRC laws, rules and regulations have established more complex procedures for acquisitions conducted by foreign investors, which could make it more difficult for us to pursue growth through acquisitions.***

The M&A Rules established certain procedures and requirements that could make mergers and acquisitions by foreign investors in China more time-consuming and complex. In addition, PRC national security review rules, which became effective on September 1, 2011, subject acquisitions by foreign investors of PRC companies that conduct business in military related or certain other industries that are crucial to national security to a security review before the consummation of any such acquisition. Furthermore, the PRC Antitrust Law, which became effective on August 1, 2008, requires, among other things, that the MOFCOM be notified in advance of any change-of-control transaction in which a foreign investor acquires control of a PRC domestic enterprise or a foreign company with substantial PRC operations, if certain thresholds set forth in the Provisions on Thresholds for Prior Notification of Concentrations of Undertakings issued by the State Council on August 3, 2008 are triggered.

We may grow our business in part by pursuing potential strategic acquisitions that are complementary to our business and operations. Complying with the requirements of these PRC laws, rules and regulations to complete such acquisitions could be time-consuming, and any required approval procedures, including obtaining approvals from the MOFCOM, may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share.

***Natural disasters and health hazards in the PRC may severely disrupt our business and operations and may have a material adverse effect on our financial condition and results of operations.***

In May 2008, a major earthquake registering 8.0 on the Richter scale struck Sichuan Province and certain other parts of China, devastating much of the affected areas and causing tens of thousands of deaths and widespread injuries. In 2010, another major earthquake registering 7.1 on the Richter scale struck Qinghai Province. In addition, in early 2008, parts of Mainland China, in particular its southern, central and eastern regions, experienced what was reportedly the most severe winter weather in the country in half a century, which resulted in significant and extensive damage to factories, power lines, homes, automobiles, crops and other properties, blackouts, transportation and communications disruptions and other losses in the affected areas. Moreover, certain countries and regions, including China, have encountered incidents of the H5N1 strain of bird flu, or avian flu, as well as severe acute respiratory syndrome, or SARS, over the past six years, and more recently in 2009, the outbreak of influenza (H1N1). We are unable to predict the effect, if any, that any future natural disasters and health and public security hazards may have on our business. Any future natural disasters and health and public security hazards may, among other things, significantly disrupt our ability to adequately staff our business, and may generally disrupt our operations. Furthermore, such natural disasters and health and public security hazards may severely restrict the level of economic activity in affected areas, which may in turn materially and adversely affect our business and prospects. As a result, any natural disasters or health hazards in China may have a material adverse effect on our financial condition and results of operations.

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## **Table of Contents**

***The implementation of the PRC Labor Contract Law may increase our operating expenses and adversely affect our business and results of operations.***

The PRC Labor Contract Law, as amended, and its implementation rules formalize workers' rights concerning overtime hours, pensions, layoffs, employment contracts and the role of trade unions and provide for specific standards and procedure for the termination of an employment contract. In addition, the Labor Contract Law requires the payment of a statutory severance pay upon the termination of an employment contract in most cases, including in cases of the expiration of a fixed-term employment contract. As there has been little guidance as to how the Labor Contract Law will be interpreted and enforced by the relevant PRC authorities, there remains substantial uncertainty as to its potential impact on our business and results of operations. The implementation of the Labor Contract Law may increase our operating expenses, in particular our personnel expenses and labor service expenses. In the event that we decide to significantly reduce the number of our employees or otherwise change our employment or labor practices, the Labor Contract Law may also limit our ability to effect these changes in a manner that we believe to be cost-effective or desirable, which could materially and adversely affect our business, financial condition and results of operations.

***Our auditor, like other independent registered public accounting firms operating in the PRC, is not inspected by Public Company Accounting Oversight Board, and as such, investors may be deprived of the benefits of such inspection.***

Our independent registered public accounting firm that issues the audit reports included in our annual reports on Form 20-F filed with the U.S. Securities and Exchange Commission, or the SEC, as external auditors of companies that are traded publicly in the United States and as a firm registered with the Public Company Accounting Oversight Board (United States), or the PCAOB, is required by the laws of the United States to undergo regular inspections by the PCAOB to assess its compliance with the laws of the United States and professional standards. As our independent registered public accounting firm is located in the PRC, a jurisdiction where the PCAOB is currently unable to conduct inspections without the approval of the PRC authorities, our auditor, like other independent registered public accounting firms operating in the PRC, is not currently inspected by the PCAOB.

Inspections of other independent registered public accounting firms that the PCAOB has conducted outside the PRC have identified deficiencies in the audit procedures and quality control procedures of those firms, which may be addressed as part of the inspection process to improve future audit quality. The lack of PCAOB inspections in the PRC prevents the PCAOB from regularly evaluating our auditor's audits and its quality control procedures. And the inability of the PCAOB to conduct inspections of independent registered public accounting firms in the PRC makes it more difficult to evaluate the effectiveness of our external auditor's audit procedures or quality control procedures as compared to external auditors outside the PRC that are subject to PCAOB inspections. As a result, investors may be deprived of the benefits of the PCAOB inspections.

### **Risks Relating to the ADSs**

***The trading price of our ADSs has been and may continue to be volatile, which could result in substantial losses to you.***

The trading price of our ADSs has been volatile and subject to wide fluctuations. Since October 5, 2007, the closing prices of our ADSs on the NYSE have ranged from US\$1.68 to US\$51.08 per ADS and the last reported sale price on April 15, 2013 was US\$1.74. Our ADSs may continue to fluctuate in response to various factors beyond our control. The financial markets in general, and the market prices for many other PRC companies listed on stock exchanges in the United States in particular, have experienced extreme volatility. These broad market and industry factors may significantly affect the market price and volatility of our ADSs, regardless of our actual operating performance.

In addition to market and industry factors, the price and trading volume for our ADSs may be highly volatile for specific business reasons. In particular, factors such as variations in our revenues, earnings and cash flow, announcements of new investments and cooperation arrangements or acquisitions could cause the market price for our ADSs to change substantially. Any of these factors may result in large and sudden changes in the volume and trading price of our ADSs. In the past, following periods of volatility in the market price of a company's securities, shareholders have often instituted securities class action litigation against that company. If we were involved in a class action suit, it could divert the attention of senior management, and, if adversely determined, have a material adverse effect on our financial condition and results of operations.

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## **Table of Contents**

***The sale or availability for sale of substantial amounts of our ADSs could adversely affect their trading price and could materially impair our future ability to raise capital through offerings of our ADSs.***

Sales of substantial amounts of our ADSs in the public market, or the perception that these sales could occur, could adversely affect the market price of our ADSs and could materially impair our future ability to raise capital through offerings of our ADSs.

As of March 31, 2013, we had 59,101,566 ordinary shares outstanding (excluding 421,526 ordinary shares that were issued and held for our account in preparation for exercise of share options by option holders under our employee stock incentive plans), including 30,675,560 ordinary shares represented by 30,675,560 ADSs (excluding the 421,526 ADSs that were held for our account in preparation for exercise of share options by option holders under our employee stock incentive plans). All ADSs are freely transferable without restriction or additional registration under the Securities Act. The remaining ordinary shares outstanding have been available for sale, subject to volume and other restrictions that may be applicable under Rule 144 and Rule 701 under the Securities Act. In addition, we have filed registration statements on Form S-8 to register the ordinary shares to be issued to the share option holders under our employee stock incentive plans. The ordinary shares to be received by such share option holders who are not affiliated with us may be resold freely to the public market. We cannot predict what effect, if any, market sales of securities held by our significant shareholders or any other shareholder or the availability of these securities for future sale will have on the market price of our ADSs.

***Your interest in our ADSs will be diluted as a result of our stock incentive plans or other share option grants.***

As of March 31, 2013, options to purchase an aggregate of 5,303,941 ordinary shares had been granted and were outstanding under the 2005 Stock Incentive Plan, the 2008 Stock Incentive Plan, the 2010 Stock Incentive Plan and the 2012 Stock Incentive Plan. For a description of these plans, see Item 6. Directors, Senior Management and Employees B. Compensation of Directors and Senior Officers Share Options. The exercise of those options would result in a reduction in the percentage of ownership of the holders of ordinary shares and of ADSs, and therefore would result in a dilution in the earnings per ordinary share and per ADS.

***You may face difficulties in protecting your interest, and your ability to protect your rights through the United States federal courts may be limited, because we are incorporated under Cayman Islands law.***

Our corporate affairs are governed by our Second Amended and Restated Memorandum and Articles of Association, the Cayman Islands Companies Act and the common law of the Cayman Islands. The rights of shareholders to take action against the directors and actions by minority shareholders are to a large extent governed by the common law of the Cayman Islands. Cayman Islands law in this area may not be as established and may differ from provisions under statutes or judicial precedent in existence in the United States. As a result, our public shareholders may face different considerations in protecting their interests in actions against our management or directors than would shareholders of a corporation incorporated in a jurisdiction within the United States.

The rights of shareholders and the responsibilities of management and members of the board of directors under Cayman Islands law, such as in the areas of fiduciary duties, are different from those applicable to a company incorporated in a jurisdiction of the United States. For example, the Cayman Islands courts are unlikely:

to recognize or enforce against us judgments of courts of the United States based on the civil liability provisions of United States federal securities laws; and

in original actions brought in the Cayman Islands, to impose liabilities against us based on the civil liability provisions of United States federal securities laws that are penal in nature.

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## **Table of Contents**

As a result, our public shareholders may have more difficulty in protecting their interests in connection with actions taken by our management or members of our board of directors than they would as public shareholders of a company incorporated in the United States.

### ***Certain judgments obtained against us by our shareholders may not be enforceable.***

We are a Cayman Islands company and substantially all of our assets are located outside of the United States. Substantially all of our current operations are conducted in the PRC. In addition, most of our directors and officers are nationals and residents of countries other than the United States. A substantial portion of the assets of these persons are located outside the United States. As a result, it may be difficult or impossible for you to bring an action against us or against these individuals in the United States in the event that you believe that your rights have been infringed under the United States federal securities laws or otherwise. Even if you are successful in bringing an action of this kind, the laws of the Cayman Islands and of the PRC may render you unable to enforce a judgment against our assets or the assets of our directors and officers.

### ***Your voting rights as a holder of our ADSs are limited by the terms of the deposit agreement.***

You may exercise your voting rights with respect to the ordinary shares underlying your ADSs only in accordance with the provisions of the deposit agreement. Upon receipt of voting instructions from you in the manner set forth in the deposit agreement, the depositary for our ADSs will endeavor to vote your underlying ordinary shares in accordance with these instructions. Under our Second Amended and Restated Memorandum and Articles of Association and Cayman Islands law, the minimum notice period required for convening a general meeting is 15 days. When a general meeting is convened, you may not receive sufficient notice of a shareholders' meeting to permit you to withdraw your ordinary shares to allow you to cast your vote with respect to any specific matter at the meeting. In addition, the depositary and its agents may not be able to send voting instructions to you or carry out your voting instructions in a timely manner. We will make all reasonable efforts to cause the depositary to extend voting rights to you in a timely manner, but you may not receive the voting materials in time to ensure that you can instruct the depositary to vote your shares. Furthermore, the depositary and its agents will not be responsible for any failure to carry out any instructions to vote, for the manner in which any vote is cast or for the effect of any such vote. As a result, you may not be able to exercise your right to vote and you may lack recourse if your ordinary shares are not voted as you requested.

### ***The depositary for our ADSs will give us a discretionary proxy to vote our ordinary shares underlying your ADSs if you do not vote at shareholders' meetings, except in limited circumstances, which could adversely affect your interests.***

Under the deposit agreement for our ADSs, the depositary will give us a discretionary proxy to vote our ordinary shares underlying your ADSs at shareholders' meetings if you do not vote, unless:

we have failed to timely provide the depositary with our notice of meeting and related voting materials;

we have instructed the depositary that we do not wish a discretionary proxy to be given;

we have informed the depositary that there is substantial opposition as to a matter to be voted on at the meeting;

a matter to be voted on at the meeting would have a material adverse impact on shareholders; or

voting at the meeting is made on a show of hands.

The effect of this discretionary proxy is that you cannot prevent our ordinary shares underlying your ADSs from being voted, absent the situations described above, and it may make it more difficult for shareholders to influence the management of our company.

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**Table of Contents**

*You may not receive distributions on our ordinary shares or any value for them if it is illegal or impractical to make them available to you.*

The depositary of our ADSs has agreed to pay you the cash dividends or other distributions it or the custodian for our ADSs receives on our ordinary shares or other deposited securities after deducting its fees and expenses. You will receive these distributions in proportion to the number of our ordinary shares that your ADSs represent. However, the depositary is not responsible if it is unlawful or impractical to make a distribution available to any holders of ADSs. For example, it would be unlawful to make a distribution to a holder of ADSs if it consists of securities that require registration under the Securities Act but that are not properly registered or distributed pursuant to an applicable exemption from registration. The depositary is not responsible for making a distribution available to any holders of ADSs if any government approval or registration required for such distribution cannot be obtained after reasonable efforts made by the depositary. We have no obligation to take any other action to permit the distribution of our ADSs, ordinary shares, rights or anything else to holders of our ADSs. This means that you may not receive the distributions we make on our ordinary shares or any value for them if it is illegal or impractical for us to make them available to you. These restrictions may have a material and adverse effect on the value of your ADSs.

*You may not be able to participate in rights offerings and may experience dilution of your holdings.*

We may, from time to time, distribute rights to our shareholders, including rights to acquire securities. Under the deposit agreement, the depositary will not distribute rights to holders of ADSs unless the distribution and sale of rights and the securities to which these rights relate are either exempt from registration under the Securities Act with respect to all holders of ADSs, or are registered under the provisions of the Securities Act. The depositary may, but is not required to, attempt to sell these undistributed rights to third parties, and may allow the rights to lapse. We may be unable to establish an exemption from registration under the Securities Act, and we are under no obligation to file a registration statement with respect to these rights or underlying securities or to endeavor to have a registration statement declared effective. Accordingly, holders of ADSs may be unable to participate in our rights offerings and may experience dilution of their holdings as a result.

*You may be subject to limitations on transfer of your ADSs.*

Your ADSs represented by ADRs are transferable on the books of the depositary. However, the depositary may close its books at any time or from time to time when it deems expedient in connection with the performance of its duties. The depositary may close its books from time to time for a number of reasons, including in connection with corporate events such as a rights offering, during which time the depositary needs to maintain an exact number of ADS holders on its books for a specified period. The depositary may also close its books in emergencies, and on weekends and public holidays. The depositary may refuse to deliver, transfer or register transfers of our ADSs generally when our books or the books of the depositary are closed, or at any time if we or the depositary thinks it is advisable to do so because of any requirement of law or any government or governmental body, or under any provision of the deposit agreement, or for any other reason.

**Item 4. Information on the Company**

**A. History and Development of the Company**

Our holding company, China Digital TV Holding Co., Ltd., was incorporated as an exempted limited liability company on April 19, 2007 under the laws of the Cayman Islands. We are headquartered in Beijing, China, and provide CA systems to the PRC's digital television market. We conduct substantially all of our business through our operating subsidiary in the PRC, Super TV, and through N-S Digital TV, a PRC company that we control through contractual arrangements. See Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions.

Our principal executive office is located at Jingmeng High-Tech Building B, 4th Floor, No. 5 Shangdi East Road, Haidian District, Beijing 100085, PRC. Our telephone number is (8610) 6297 1199. Information contained on our website does not constitute a part of this annual report. Our agent for service of process is CT Corporation System, located at 111 Eighth Avenue, New York, New York 10011, U.S.A.

## **Table of Contents**

N-T Information Engineering was established as a limited liability company under the PRC law by Tsinghua Enterprise Group, a company affiliated with Tsinghua University, and Hong Kong-based Tsinghua Novel Hi-Tech Investment Holding Ltd. in July 1998, and initially focused on developing, producing and selling digital data broadcasting equipment for cable television operators. In December 2002, N-T Information Engineering completed its acquisition of the CA systems-related assets of Tsinghua Tongfang Co., Ltd., or Tsinghua Tongfang. In March 2004, CDTV BVI was incorporated as a holding company in the British Virgin Islands, or BVI. Following the establishment of CDTV BVI, we restructured our operations, in connection with an investment by SAIF, by establishing Super TV, a limited liability company under the PRC law and a wholly-owned subsidiary of CDTV BVI, on May 31, 2004. On the same day, N-T Information Engineering and Li Yang, a PRC citizen then employed by SAIF, established N-S Digital TV. In June 2004, N-S Digital TV acquired from N-T Information Engineering its smart card and CA systems business and, in August 2006, N-S Digital TV acquired from N-T Information Engineering its set-top box design business. In April 2007, a new holding company, China Digital TV Holding Co., Ltd., or CDTV Holding, was established in the Cayman Islands. In May 2007, CDTV BVI executed a 40-for-1 share split of its ordinary shares and Series A preferred shares. Following this share split, the shareholders of CDTV BVI exchanged all of their shares of CDTV BVI for shares of CDTV Holding in proportion to their percentage interest in CDTV BVI, as a result of which CDTV BVI became a wholly-owned subsidiary of CDTV Holding. In August 2007, with our consent, Ms. Yang transferred her entire equity interest in N-S Digital TV to Wei Gao, a PRC citizen employed by an affiliated company of SAIF.

In October 2007, we completed the initial public offering of our ADSs representing our ordinary shares and listed the ADSs on the NYSE.

In order to benefit from certain beneficial tax arrangements between the PRC and Hong Kong, in December 2007, CDTV BVI acquired Golden Benefit, a company incorporated in Hong Kong, for a nominal consideration, and transferred its 100% equity interest in Super TV to Golden Benefit. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China We may be subject to PRC income tax on our global income, or dividends we receive from our PRC subsidiary may be subject to PRC withholding tax, depending on whether we are recognized as a resident enterprise in the PRC and Item 5. Operating and Financial Review and Prospects A. Operating Results Taxes and Incentives PRC.

Since December 2007, new entities have been established in the PRC to offer new solutions and products, including N-S Media Investment, Cyber Cloud, Joysee and Super Movie.

In June 2008, Ms. Gao transferred all of her equity interests in N-S Digital TV to Junming Wu, who is a PRC citizen and is currently our employee. In November 2008, N-T Information Engineering transferred all of its equity interest in N-S Digital TV, our variable interest entity, to Lei Zhang and Shizhou Shen, both of whom are PRC citizens and are currently our employees. In July 2011, Junming Wu transferred all of his equity interests in N-S Digital TV to Tianxing Wang, who is a PRC citizen and is currently our employee. In addition, in July 2011, Tianxing Wang, Lei Zhang and Wenjun Wang, who are PRC citizens and are currently our employees, each contributed cash to increase the registered capital of N-S Digital TV to RMB150 million using the loan proceeds from Super TV. As a result of these transactions, Tianxing Wang, Lei Zhang, Shizhou Shen and Wenjun Wang in aggregate own all of the equity interest of N-S Digital TV.

N-S Digital Technology Co., Ltd., or N-S Digital Technology, and N-S Investment Holdings Co., Ltd., or N-S Investment Holdings, were incorporated in the PRC as wholly-owned subsidiaries of our company in April and July 2010, respectively. In March 2011, N-S Digital Technology was dissolved.

### ***Our Investments and Acquisitions***

In August 2006, N-S Digital TV entered into an asset transfer agreement to purchase from N-T Information Engineering its set-top box design business for an initial purchase price of RMB29.4 million (US\$3.8 million), subject to certain post-closing downward adjustments. As an adjustment to the initial purchase price, N-T Information Engineering refunded RMB12.1 million (US\$1.5 million) to N-S Digital TV in April 2007. For details of the adjustment mechanism of the initial purchase price, see Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Super TV and N-S Digital TV Arrangements Transfer of Assets and Equity Interests and Intellectual Property Rights Asset Transfer Agreement, dated August 5, 2006, between N-T Information Engineering and N-S Digital TV, as amended on April 6, 2007.

**Table of Contents**

In August 2006, N-S Digital TV entered into an equity transfer agreement to purchase from N-T Information Engineering its 51% equity interest in Foshan Nanhai Guokai Digital TV Technology Co., Ltd., or Guokai, for a cash consideration of RMB2.4 million (US\$0.3 million). The parties entered into a new agreement in March 2007 to reduce the consideration to RMB2.3 million (US\$0.3 million). Guokai is a company primarily engaged in the research, development and sale of digital TV-related systems, software and products. A Japanese multinational company holds the remaining 49% equity interest in Guokai. This transaction was completed on July 27, 2007. We have decided to discontinue the business of Guokai and are in the process of dissolving Guokai.

In March 2007, N-S Digital TV and Jiangsu Qingda Technology Co. Ltd., or Jiangsu Qingda, one of our customers, entered into an agreement to set up a joint venture in Nanjing of Jiangsu Province mainly engaging in digital television technology development and services, Nanjing Qingda Yongxin Culture & Media Co. Ltd., or Qingda Yongxin. N-S Digital TV contributed cash of RMB0.8 million (US\$0.1 million), representing 40% of equity interest in the joint venture. Jiangsu Qingda contributed cash of RMB1.2 million (US\$0.2 million) representing 60% of equity interest in the joint venture. N-S Digital TV had an option to purchase up to an additional 30% of the equity interest of Qingda Yongxin, which expired in 2010 without being exercised.

In June 2008, N-S Digital TV and Xitao Lai, a PRC citizen, established Dongguan SuperTV Video Info Co., Ltd., or Dongguan SuperTV, a joint venture in Dongguan, Guangdong Province, mainly to provide value-added services to television viewers. N-S Digital TV and Mr. Lai each contributed cash of RMB5.0 million (US\$0.7 million), representing 50% of equity interest in the joint venture. In September 2008, N-S Digital TV exercised an option to purchase an additional 10% equity interest in the joint venture from Mr. Lai. In July 2009, N-S Digital TV sold its 20% equity interest in Dongguan SuperTV to a new investor, Guangdong Jiakai Digital Technology Co., Ltd., or Guangdong Jiakai. In August 2010, N-S Digital TV entered into an equity transfer agreement with Guangdong Jiakai to repurchase the 20% equity interest in Dongguan SuperTV from Guangdong Jiakai. After those transactions, the equity interest of Dongguan SuperTV held by N-S Digital TV increased to 60% and N-S Digital TV became entitled to 70% of shareholders' voting rights and appointing three out of the five members of the board of directors of Dongguan SuperTV. In November 2011, Dongguan SuperTV transferred all of its high-definition interactive television services-related assets to the Dongguan branch of the Guangdong Broadcasting TV Network Co., Ltd. In December 2011, N-S Digital TV transferred its entire equity interest in Dongguan SuperTV to a third party for total consideration of RMB6.6 million (US\$1.0 million).

In August 2008, we acquired from N-T Information Engineering all of its intellectual property rights relating to digital watermarking and image tracing technologies, including one issued patent and five pending patent applications in the PRC. For details of these acquisitions, see Item 4. Information on the Company B. Business Overview Intellectual Property and Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Super TV and N-S Digital TV Arrangements.

On January 4, 2010, we entered into a share purchase agreement with OpenV China Holdings Company, or OpenV, a PRC online video company, and several other parties to make a strategic investment in OpenV. Pursuant to the share purchase agreement and related transaction documents, we acquired an 11.5% equity interest (subject to adjustment based on, among others, OpenV's performance) in OpenV for a consideration of US\$5.0 million and received a warrant to purchase ordinary shares of OpenV of up to US\$4.5 million. As part of this investment transaction, we also agreed to extend to OpenV a US\$2.5 million interest-free convertible loan, which could be converted into ordinary shares of OpenV, subject to certain closing conditions. The Company did not purchase additional ordinary shares of OpenV pursuant to the warrant, which has expired, and the interest-free convertible loan was not extended to OpenV due to OpenV's performance in 2010. In 2010, we wrote off our entire investment in OpenV because we had doubts on OpenV's ability to continue as a going concern. As of December 31, 2012, we understood that OpenV's normal online video services had not been restored. On October 11, 2012, we entered into a share redemption agreement with OpenV, pursuant to which OpenV repurchased 460,080 of its shares from us for US\$0.82 million. We continue to hold 2,345,267 shares of OpenV after the share repurchase.

In February 2010, N-S Digital TV acquired from Beijing Shi Xun Hu Lian Technology Co., Ltd., or Beijing Shi Xun, and another shareholder of Guangdong Digital Media Technology Research & Development Institute Co., Ltd., or Guangdong R&D, their entire equity interest in Guangdong R&D for RMB3.0 million (US\$0.4 million) and became the sole shareholder of Guangdong R&D. We have decided to discontinue the business of Guangdong R&D and are in the process of dissolving Guangdong R&D.

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**Table of Contents**

In May 2010, we entered into a share subscription agreement with 3DiJoy Corp., or 3DiJoy, a company specializing in the research and development of interactive and motion-sensing gaming products, and several other parties to make a strategic investment in 3DiJoy. Pursuant to the share subscription agreement, we acquired an aggregate of 4,953,798 series C convertible preferred shares of 3DiJoy, representing a 24% equity interest, for an aggregate subscription price of US\$6.0 million. In 2012, we accrued a full impairment charge of US\$4.5 million related to our investment in 3DiJoy based on the fair value of 3DiJoy we estimated with the assistance of a third party valuation firm, as we had doubts regarding 3DiJoy's ability to operate as a going concern given that it had been experiencing financial difficulties and had failed to obtain new capital funding from its shareholders or otherwise.

In May 2010, Super TV acquired an aggregate 34.45% equity interest in Guangzhou Rujia Network Technology Co., Ltd., or Guangzhou Rujia, through both purchase of existing shares from a shareholder of Rujia and contribution to its capital increase, for total consideration of RMB16.5 million (US\$2.5 million).

In August 2010, N-S Digital TV entered into an equity transfer agreement with Guangzhou Rujia to transfer all of its equity interest in Guangdong SuperTV for a consideration of RMB30.3 million (US\$4.6 million).

In December 2010, Super TV and Beijing Yuewu Yuntian Software Technology Ltd., or Yuewu Yuntian, agreed to establish Beijing Cyber Cloud Co., Ltd., or Cyber Cloud, in Beijing mainly engaging in research and development of cloud computing technology-based digital video delivery solutions. Super TV and Yuewu Yuntian contributed cash of RMB45.0 million (US\$6.8 million) and RMB5.0 million (US\$0.8 million), representing 90% and 10% of the equity interest in Cyber Cloud, respectively. Cyber Cloud was formally established on January 19, 2011.

In April 2011, Super TV and Beijing Ying Zhi Cheng Technology Co., Ltd., or Ying Zhi Cheng Technology, agreed to establish Joysee in Beijing, which mainly engages in the research and development of advanced digital television terminals. Super TV and Ying Zhi Cheng Technology contributed cash of RMB27.0 million (US\$4.2 million) and RMB3.0 million (US\$0.5 million), representing 90% and 10% of the equity interest in Joysee, respectively. Pursuant to an agreement, dated May 24, 2011, among Super TV, N-S Digital TV and Ying Zhi Cheng Technology, N-S Digital TV contributed RMB6.0 million (US\$0.9 million) in cash, representing a 16.7% equity interest in Joysee. Pursuant to an agreement, dated June 13, 2011, among Super TV, N-S Digital TV, Ying Zhi Cheng Technology and Intel Semiconductor (Dalian) Ltd., or Intel, a wholly-owned subsidiary of Intel Corporation in the PRC, Intel contributed RMB33.0 million (US\$5.1 million) in cash, representing a 37.5% equity interest in Joysee. Pursuant to an equity transfer agreement, dated June 13, 2011, between N-S Digital TV and Intel, Intel transferred 7.5% of its equity investment in Joysee to N-S Digital TV for a nominal consideration. As a result of these transactions, Super TV, N-S Digital TV, Ying Zhi Cheng Technology and Intel each holds a 46.9%, 17.9%, 5.2% and 30% equity interest in Joysee, respectively.

In June 2011, Super TV and Beijing AirMedia Advertising Co., Ltd., or AirMedia, entered into a framework cooperation agreement for the establishment of two joint ventures, Beijing Shibo Movie Technology Co., Ltd., or Shibo Movie, and Beijing Xinghe Union Media Co., Ltd., or Xinghe Union, in the PRC, each of which mainly engages in movie-related content sourcing and distribution services. In December 2011, Super TV, N-S Digital TV and AirMedia entered into a supplemental agreement, pursuant to which Super TV transferred its rights and obligations under the framework cooperation agreement to N-S Digital TV. N-S Digital TV and AirMedia each contributed in cash RMB5.0 million (US\$0.8 million), representing 50% of the equity interest in Shibo Movie, and cash of RMB5.0 million (US\$0.8 million), representing 50% of the equity interest in Xinghe Union. Shibo Movie and Xinghe Union were formally established on February 15, 2012 and March 13, 2012, respectively.

In August 2011, Super TV and Beijing Chaoying Weichuang Technology Ltd. agreed to establish Super Movie, which mainly engages in video program delivery services. Super TV and Beijing Chaoying Weichuang Technology Ltd. contributed cash in the amount of RMB13.5 million (US\$2.1 million) and RMB1.5 million (US\$0.2 million), respectively, representing 90% and 10% of the equity interest in Super Movie, respectively. Super Movie was formally established on September 23, 2011. We have decided to discontinue the business of Super Movie and are in the process of dissolving Super Movie.

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## **Table of Contents**

### ***Capital Expenditures and Divestitures***

See Item 5. Operating and Financial Review and Prospects B. Liquidity and Capital Resources Capital Expenditures for information concerning our principal capital expenditures for the previous three years and those currently in progress. We have not undertaken any significant divestitures.

## **B. Business Overview**

### **Overview**

We are the leading provider of CA systems to the PRC's digital television market. Our CA systems, which consist of smart cards, head-end software for television network operators and terminal-end software for set-top box manufacturers, enable digital television network operators in the PRC to control the distribution of content and value-added services to their subscribers and block unauthorized access to their networks. As of December 31, 2012, we had installed CA systems at 385 digital television network operators in 29 of the 32 provinces, autonomous regions and centrally administered municipalities in the PRC. We were the leading vendor of smart cards for CA systems in terms of smart cards shipped in the PRC in 2012, with a market share of approximately 58.6%, according to ResearchDTV. We derive a substantial majority of our revenues from sales of our smart cards, which accounted for 91.5% and 83.3% of our total revenues in 2011 and 2012, respectively. We expect that the sales of our smart cards will continue to constitute the majority of our revenues in the near future. In addition, we sell advanced digital television application software such as electronic program guides and subscriber management systems to digital television network operators. We are also developing and commercializing certain new solutions and products, including value-added digital television services, cloud computing technology-based digital video delivery solutions and advanced digital television terminals. Furthermore, we have been installing CA systems outside the PRC since 2010, including countries such as Thailand and India.

PRC television network operators are in the process of migrating from analog to digital transmissions, and the PRC government has set a target of 2015 for cable television operators to complete their digital transition. We are a primary beneficiary of this transition because CA systems are an essential component of any pay-television platform. We sell our CA systems and digital television application software to PRC television network operators, including cable, mobile, satellite and terrestrial television network operators, enterprises that maintain private cable television networks within their facilities and media operators.

Our top five customers in terms of revenues in 2012 were Jiangsu Qingda, GMM One Sky Co., Ltd., Heilongjiang Broadcasting TV Network Co., Ltd., Chongqing Cable TV Network Co., Ltd. and Sichuan Cable TV Network Co., Ltd., Chengdu Branch, which in aggregate contributed 21.0% of our total revenue in 2012.

We were founded in 2004 by Dr. Zengxiang Lu and Jianhua Zhu, who had worked together since 2001 at N-T Information Engineering, one of the PRC's earliest CA systems vendors. We purchased N-T Information Engineering's CA systems business in 2004 and continued to build upon the strong reputation that business had achieved. Our net revenues were US\$87.1 million, US\$99.1 million and US\$88.7 million in 2010, 2011 and 2012, respectively. We sold 16.2 million, 18.3 million and 15.3 million smart cards in 2010, 2011 and 2012, respectively. Our net income was US\$33.4 million, US\$40.3 million and US\$5.5 million in 2010, 2011 and 2012, respectively.

### **Our Products and Services**

Our core products and services include the following:

end-to-end CA systems, including smart cards, head-end software and terminal-end software;

other digital television application software for television network operators; and

other products.

## **Table of Contents**

### ***CA Systems***

Our CA systems consist of: software that is installed at the premises of the television network operator, or the head end; software that is installed in a set-top box at the subscriber's end, or the terminal end; and smart cards that are inserted into the set-top boxes. At both the head end and the terminal end, our CA systems are designed to interface easily with the software and hardware of as many other vendors as possible. This gives our customers maximum flexibility in selecting the components of their digital transmission systems, and allows us to cooperate with the other vendors in promoting each other's products to the network operators.

Our CA systems give cable television network operators the flexibility to charge subscribers on a per-channel or per-view basis, and to restrict viewers from making copies of the programs they watch. Our CA systems also support or offer the following functions:

***Video on demand.*** Video on demand is a system that allows subscribers to select and watch video on demand and provides subscribers with a large subset of personal-video-reorder functions, such as pause, fast forward, slow forward and jump to previous/future frame. Television network operators need to have two-way transmission capacity in order to apply such systems, which either stream content through a set-top box for viewing in real time, or download the content to subscribers' local storage devices for viewing at any time.

***Near video-on-demand.*** Television network operators who do not yet have two-way transmission capacity, which is necessary for full-blown video on demand, can broadcast the same program repeatedly at short intervals, typically of 10 to 20 minutes, giving subscribers many choices of time to start watching the program.

***Push video-on-demand.*** Television network operators who do not yet have two-way transmission capacity can record programs onto subscribers' local storage devices based on subscribers' instructions, giving subscribers the flexibility to watch the programs at time of their own choice.

***Personal video recorder.*** A personal video recorder, or digital video recorder, is a device that records video in a digital format to a disk drive or other memory medium within the device. Access to the contents, such as television programs, recorded in the personal video recorder is controlled by the CA system module and the smart card installed in the personal video recorder.

***Parental control.*** Parents can use the set-top box to set viewing controls by creating a password that must be entered to watch television or to watch certain programs, and can block access to the system at certain hours.

***Location control.*** Television network operators can authorize each smart card and set-top box to function only on the premises of the subscriber in whose name the smart card and set-top box are registered, preventing subscribers from providing their smart cards and set-top boxes to others.

***E-wallets.*** Information about pre-payment by subscribers for programs or services can be recorded on their smart cards. As subscribers order programs or services, the fees are deducted from the amounts recorded on their smart cards.

***Messaging.*** Network operators can communicate with their subscribers by transmitting electronic messages about bill status, rate changes and new programs and services to their subscribers' televisions. Network operators also can allow other vendors, such as water or electricity companies, to send billing or other service messages via this messaging platform.

***Upgrades.*** CA systems upgrades can be accomplished by transmitting software over the transmission network to the terminal end.



## **Table of Contents**

We guarantee the security of the encryption technologies of our CA systems during the periods generally ranging from one to three years after sale. In the event of a security problem, we undertake to attempt to resolve the problem by taking steps such as resetting the encryption code or adding additional layers of encryption. If these or other system modifications do not resolve the problem, we undertake to replace our smart cards. Upon expiration of the applicable period, the customer bears some portion or all of the cost. To date, we have not encountered any material problems with the security of our CA systems.

**Smart Cards.** Our smart cards are manufactured by third-party manufacturers based on our blueprints, and then are encoded by us on our premises with security codes unique to each customer. We forward the chips to smart card manufacturers in the PRC, which embed the chips in plastic cards. When we receive the cards from the card manufacturers, we program each one with a unique security code so that it can communicate with the CA systems of its intended network. We currently have enough equipment and trained staff to encode 100,000 smart cards on our premises during an eight-hour shift. An additional layer of security code is added at the customer's premises using software that we install as part of our CA systems.

Our customers generally wait until after they have purchased, installed and tested our head-end CA systems software before placing purchase orders for smart cards. We may offer discounts for large smart card orders. We sold 16.2 million, 18.3 million and 15.3 million smart cards in 2010, 2011 and 2012, respectively.

Our smart cards are manufactured to meet the ISO-7816 standard for card readability. We guarantee the quality of our smart cards for periods generally ranging from one to three years and if any of our cards are found to have defects during the applicable warranty period, we replace them for free. To date, we have not experienced a material rate of smart card failure.

**Head-End Software.** Our head-end software includes: an entitlement management message generator, which notifies the smart card whether the subscriber is entitled to view a program or not; an entitlement control message generator, which sends messages that the set-top box uses to unscramble the digital television signal; and encryption software, which encrypts the outgoing messages.

Our head-end software also includes simulcrypton software that allows network operators to install parallel CA systems from multiple vendors and transmit their programs to some subscribers using one CA system's security codes and to other subscribers using another CA system's security codes. Many of the cable television network operators in the PRC who use digital transmission have installed two or more CA systems sourced from different vendors in order to reduce dependency on a single vendor. Moreover, in 2003, the SARFT issued a policy requiring digital cable television network operators who install non-PRC CA systems to also install a domestic CA system. Our simulcrypton software and open-interface technology enable us to work with operators to install parallel CA systems, and we have integrated our CA systems with those of NDS Group, Irdeto Access BV, Sumavision Technologies Co., Ltd. and DVN Holdings Ltd., among others.

As of December 31, 2012, our CA systems had been installed at 385 digital television network operators.

We generally install, customize, test and commission our CA systems over a period of months and train our customers' staff to operate it. Our prices vary according to the size and complexity of each customer's network, as well as market conditions. Generally, the contract price is payable in installments with the respective installments due on issuance of a preliminary acceptance, issuance of a final acceptance or within a certain period thereafter, or, in the case of a single acceptance, due prior, on and/or after the issuance of the acceptance.

**Terminal-End Software.** We license our CA systems terminal-end software to whichever set-top box manufacturer has been chosen by our customer to produce set-top boxes compatible with our CA systems. More than 150 set-top box manufacturers in the PRC have installed our technology in their set-top boxes.

Once our customer has selected one or more set-top box manufacturers, the selected manufacturers enter into contracts with us to license our terminal-end software for use in their manufacturing processes so that their set-top boxes can be used on the planned network. The manufacturers agree to pay us a one-time license fee, including fees for testing and certifying their set-top boxes, and royalties for each box they manufacture using our software. We have also entered into agreements with certain television network operators who purchase our CA systems pursuant to which the operators agree to pay us royalties for each set-top box deployed on their networks that uses our CA systems terminal-end software.

## **Table of Contents**

### ***Other Digital Television Application Software for Television Network Operators***

Our other digital television application software for television network operators primarily includes subscriber management systems and electronic program guides.

***Subscriber Management Systems.*** We produce subscriber management system, or SMS, software, which can be used by television network operators to reduce the cost and improve the efficiency of their subscriber management. Our SMS software is compatible with the CA systems of other vendors, and we sell it on a stand-alone basis as well as packaged with our CA systems. Our SMS software performs the following functions:

maintains and updates a database of subscriber information;

processes subscriber orders for new services;

maintains billing, payment and authorization records and sends e-mail bills and receipts to subscribers; and

processes subscriber requests to repair or replace defective or lost set-top boxes or smart cards.

As of December 31, 2012, our SMS software had been installed by 117 television network operators. Our prices vary according to the size and complexity of each customer's network, as well as market conditions.

***Electronic Program Guides.*** An electronic program guide is an on-screen guide to the programs and services available to subscribers. Our electronic program guide is a software application that is installed at the head end of a CA system and can be controlled by a remote control. Viewers can use the guide to obtain program schedules as well as information about specific programs, such as plot descriptions and the names of featured actors.

As of December 31, 2012, our electronic program guide had been installed by 208 television network operators. Our electronic program guide may be sold together with our CA systems, but it is also compatible with the CA systems of other vendors. When we sell our electronic program guides packaged with our CA systems, we provide the same maintenance terms as for the CA systems. Our prices vary according to the size and complexity of each customer's network, as well as market conditions.

### ***Other Products***

We sell other products sourced from third party suppliers, such as integrated chips, surface mounted device chips and multimedia home entertainment boxes.

***Integrated chips.*** Integrated chips are special module chips which highly integrated the main components of set-top box main board and may be used in small-sized and diversified electronic products. We provide our customers with integrated chips for set-top boxes that have been made to our specifications by third party manufacturers. We sold 4,000, 54,000 and 87,000 integrated chips in 2010, 2011 and 2012, respectively.

***Surface mounted device chips.*** Surface mounted device chips are of similar function as smart cards, except that surface mounted device chips are not embedded in plastic cards. Surface mounted device chips may be packed in different forms and are widely used in different kinds of terminals. We sold 0.7 million and 1.8 million surface mounted device chips in 2011 and 2012, respectively.

***Multimedia home entertainment boxes.*** Multimedia home entertainment boxes are triple play terminals that provide consumers with tri-networks integration applications, such as digital television, IPTV, high speed internet access, video calls and somatic games. As of December 31, 2012, our multimedia home entertainment boxes had been sold to more than ten television network operators.



## **Table of Contents**

### **Technical Support and Services**

We offer system integration services for television network operators who are digitalizing and installing our CA systems. As system integrators, we purchase additional hardware and software from third parties and integrate it with our CA systems software. If our customers install multiple CA systems from more than one vendor, we integrate these systems with our own so that all the hardware and software operate as a seamless whole.

As of December 31, 2012, we had a total of 58 technicians and engineers located in Beijing and two other cities available 24 hours a day to respond to customer requests for information and assistance. Our two regional service centers are strategically located in eastern (Hangzhou) and southern (Nanhai) China. Each service center maintains a 24-hour telephone hotline. Upon receiving a call for assistance, our technical support employees first attempt to identify and resolve the problem over the telephone or by accessing the software remotely, and then arrange a site visit if necessary. In addition, each customer is assigned a project manager who oversees the initial software installation and remains primarily responsible for ensuring that after-sale requests for assistance are handled promptly.

### **Sales and Marketing**

As of December 31, 2012, we had 168 full-time sales personnel. We maintain regular contact with our customer base through contacts at industry forums and sales visits, and use these opportunities to educate them about digital television systems. We actively monitor which operators are moving towards digitalization, and when we learn that a particular operator is planning to launch a digital network, we target that operator for more frequent contact by our sales and technical personnel. We compensate our sales personnel by means of base salaries and performance bonuses.

We also cooperate informally with other providers of digital television software and hardware with whom we do not compete, such as set-top box manufacturers, to promote each other's products to our respective customers, and thereby benefit from each other's marketing efforts.

Jiangsu Qingda, a Nanjing-based company, is our exclusive distributor for CA systems and smart cards in Jiangsu Province in eastern China. Jiangsu Qingda also provides after-sales technical support and maintenance services for our customers in Jiangsu Province. We entered into a 13-year distribution contract with Jiangsu Qingda effective January 1, 2007. We account for revenues contributed by Jiangsu Qingda in the same way as revenues from our customers who are television network operators. Jiangsu Qingda was our largest contributor to revenues in 2010, 2011 and 2012. In addition to Jiangsu Qingda, we also engage fee-based sales agents to assist us in selling and maintaining our CA systems and smart cards in designated regions or to designated customers. Such sales agents also provide certain related services, including gathering market intelligence regarding potential customers and pricing information in the relevant market.

### **Customers**

Our primary customers are cable television network operators. We sell our products and services to networks of all sizes. Our top five customers in 2012 were Jiangsu Qingda, GMM One Sky Co., Ltd., Heilongjiang Broadcasting TV Network Co., Ltd., Chongqing Cable TV Network Co., Ltd. and Sichuan Cable TV Network Co., Ltd., Chengdu Branch, which contributed 9.4%, 3.8%, 2.8%, 2.6% and 2.4%, respectively, to our total revenues for the year.

We have also sold our CA systems to:

satellite and terrestrial television network operators, including the China Central Satellite Television Transmission Center;

a commercial satellite transmission platform, namely China Dbstar Co., Ltd.;

## **Table of Contents**

large enterprises that maintain private cable television networks within their facilities, including the Beijing Capital International Airport and Daqing Oilfield Company Limited, a wholly-owned subsidiary of PetroChina Company Limited;

media operators who use CA systems to encrypt their programs for distribution to television operators, including China DTV Media Inc., Ltd. and Huacheng Digital Movie & TV Co., Ltd.; and

a mobile television operator, namely China Broadcasting (Group) Co., Ltd. (formerly known as China Satellite Mobile Broadcasting Corporation or China Broadcasting Co., Ltd.).

We currently derive, and we expect to continue to derive, a significant portion of our revenues each period from a limited number of large customers, although the particular customers may vary from period to period. As digital cable television systems are at the developing stage in the PRC, the largest shipments of smart cards are to operators who are launching new digital transmission systems and need to purchase in bulk for their established networks. For example, Jiangsu Qingda was our only customer that contributed more than 10% of our total revenues in 2010, representing 14.2% of our revenues in that year. We may face certain risks from this concentration of revenues. See Item 3. Key Information D. Risk Factors Risks Relating to Our Business and Industry We depend, and expect to continue to depend, on a limited number of customers for a significant portion of our revenues in any single period. If one customer defers or cancels its orders or chooses our competitors products or services, our revenues and net income could decline significantly.

As most cable television network operators in the PRC are state-owned, they are required to follow a public bidding process for major purchases. As a result, the majority of our CA systems sales are made pursuant to a formal bid process. In such cases, the network operator generally submits its CA systems requirements to a state-owned bidding company, which posts a request for bids at its Internet site and specifies the necessary financial and technical qualifications of bidders. We are generally required to accompany our bid with a cash deposit, which generally is from US\$300 to US\$117,000 and which is refundable in full if we fail to win the sales contract. If we succeed in winning the contract, some network operators require that we leave our deposit in their account until we have installed and tested our software and the network operator has signed a certificate of acceptance. The time from when a request for bids is posted until a winner is selected is usually one to two months.

Our customers also include set-top box manufacturers, to whom we license terminal-end software for our CA systems. More than 150 set-top box manufacturers in the PRC, including Coship Electronics Co., Ltd., Huawei Technologies, Hangzhou Motorola Technologies Ltd., Skyworth, TCL Technology, Jiuzhou Electric Co., Ltd., Changhong Electric Co., Ltd., Intel Corporation and Hisense, have installed our terminal-end software in their set-top boxes.

## **Suppliers**

Before 2006, we bought most of our computer chips for our smart cards from STM. In order to maintain a secure supply of computer chips, beginning in 2006 we have purchased a significant portion of our computer chips from Infineon, initially indirectly through AdvanIDE Pte. Ltd. (formerly known as ACG Identification Technologies Asia Pte. Ltd.), an agent of Infineon, and since February 2009, directly from Infineon.

STM and Infineon produce chips that use our card operating system and deliver them to Beijing by air freight. We do not have long-term contracts with any of our computer chip suppliers, but place orders according to our customers' demands. We pay based upon the prevailing market price at the time of order.

The time required from placing a new chip order with the fabricators to shipping finished smart cards to our customers may be as long as 15 weeks. To ensure that we are able to meet our customers' demands, we plan at all times to have enough chips and smart cards on order or in inventory to meet our demand for an average 15-week period.

We have arrangements with a number of smart-card manufacturers, including China Electronics, the China Sciences Group and Axalto Smart Card Technology Co., to embed the computer chips into plastic cards. We currently maintain a one-year contract with each of China Electronics and the China Sciences Group that guarantees us a volume-based price discount for each purchase order and requires China Electronics or the China Sciences Group, as the case may be, to fulfill our orders in accordance with an agreed schedule. We do not have any long-term contract with Axalto Smart Card Technology Co. Our contracts with China Electronics and the China Sciences Group require them to meet the ISO-7816 standard for card readability. In addition, we believe that there are numerous alternative smart-card manufacturers from whom we would be able to obtain smart cards if any of our current suppliers were unable to meet our needs.



## **Table of Contents**

For more information about risks relating to our relationships with our suppliers, see Item 3. Key Information D. Risk Factors Risks Relating to Our Business and Industry We generally do not have long-term contracts with suppliers of computer chips or the companies that manufacture our smart cards. If any of our computer chip suppliers or smart-card manufacturers is unable to fulfill our orders in time or at all, we may be unable to deliver smart cards to our customers, which could have a material adverse effect on our business, financial condition and results of operations.

### **Competition**

We face competition in the CA systems market from both international and domestic companies. We compete on the basis of:

customer service and technical support;

brand name, track record and market recognition;

encryption management and other technologies, including our smart cards;

the number of set-top box manufacturers with whom we cooperate; and

price.

Our main international competitors in the CA systems business are Irdeto Access B.V., Conax Company and Kudelski SA. These companies have longer operating histories and substantially greater financial, technical and other resources than we do, which may enable them to respond more quickly than we could to technological or commercial changes in our industry. In addition, several of these companies entered the PRC market before us, but have to date been less successful in capturing market share. Historically, these companies have generally focused on sales to the television network operators in the PRC's largest cities. To the extent that our international competitors may begin targeting small- and mid-size television network operators, we believe that we can continue to compete successfully because of our local knowledge and relationships and our more extensive customer support and service network.

Our main domestic competitors are Sumavision Technologies Co., Ltd. and DVN Holdings Ltd., both of which are non-state-owned companies operating mainly in the PRC. They may offer their CA systems at a lower price or with a longer credit term than we do. However, we believe that we have more advanced technology than they do, and that our strong technology and leading market position will enable us to continue to compete successfully against these companies.

According to Researchdvtv, we were the leader in the PRC CA systems market in 2011 and 2012. According to Researchdvtv, in 2012, we had an approximately 58.6% market share based on the number of smart cards shipped, followed by Sumavision Technologies Co., Ltd. with approximately 12.6% market share, DVN Holdings Ltd. with approximately 12.1% market share, Irdeto Access B.V. with approximately 6.6% market share, Conax Company with approximately 2.3% market share, Kudelski SA with approximately 1.1% market share and others accounting for the remaining 6.7%. For more information about risks relating to our competitors, see Item 3. Key Information D. Risk Factors Risks Relating to Our Business and Industry We face intense competition, which could reduce our market share and harm our financial performance.

## **Table of Contents**

### **Research and Development**

Our success to date has in large part resulted from our strong research and development capabilities. As of December 31, 2012, our research and development team consisted of 439 employees, compared to 334 as of December 31, 2011 and 308 as of December 31, 2010. Our research and development expenses increased from US\$10.4 million in 2010 to US\$13.1 million in 2011 and US\$17.4 million in 2012.

Our business and the market in which we operate are characterized by rapid technological change, evolving industry standards and frequent product enhancements. As digital broadcasting becomes more popular in the PRC, television network operators are likely to seek more sophisticated CA technology that offers them greater reliability, flexibility and functionality in delivering protected content or value-added services to viewers. As methods of distributing information and entertainment evolve, CA technology also needs to evolve to provide content protection for distribution platforms other than television. Our continued success will depend, in part, on our ability to develop and market products and services that respond to technological changes and evolving market demand or industry standards in a timely and cost-effective manner.

Many of our current research and development staff are graduates of the PRC's top science and engineering universities, including Tsinghua University, and have extensive experience in digital television and encryption technologies. Our research team played a leading role in drafting the PRC industry standards for CA systems, electronic program guides and other key industry standards. We are active in the China Digital Rights Management Forum, which aims to develop a PRC standard for digital rights management.

Our research and development personnel are actively seeking ways to improve the security and reliability of our CA systems, as well as to prevent content theft at other stages of the television network operators' chain of transmission. Other focuses of our research include: (1) adapting our CA systems for use on new television platforms, such as satellite television, mobile television, IPTV and Internet TV; (2) enhancing our CA systems to support applications such as video-on-demand, near video-on-demand, push video-on-demand and personal video recorders; (3) developing new value-added services that will enhance operator revenues; (4) developing a new line of products and technologies, including high-definition and hybrid set-up box solutions and digital rights management products that allow content providers to control the way their content is distributed and reproduced, such as advanced digital television terminals; (5) applying cloud computing to television applications; and (6) developing our CA systems for use outside of the PRC.

### **Intellectual Property**

We develop all of our software internally, and our proprietary intellectual property is critical to our success. We rely primarily on a combination of patent, trademark and copyright laws, trade secrets, licenses and employee and third-party confidentiality agreements to safeguard our intellectual property. We generally enter into confidentiality and non-disclosure agreements with our employees, customers and suppliers.

As of December 31, 2012, we had a total of 69 patents issued and 73 pending patent applications in the PRC. Our issued patents and pending patent applications relate primarily to digital transmission technologies, encryption and decryption technologies, technologies relating to the production of set-top boxes and smart cards and technologies relating to value-added services. We have also completed copyright registration of 89 software programs, and have pending copyright registration applications for two software programs, relating to digital television in the PRC.

In August 2008, we acquired from N-T Information Engineering all intellectual property rights relating to the digital watermarking and image tracing technologies, including one issued patent and five then pending patent applications in the PRC. Four of these pending patent applications relate to the digital watermarking technology, while the remaining pending patent application and the issued patent relate to the image tracing technology. The digital watermarking technology is aimed to enhance cable television operators' counterfeit tracking and broadcasting restriction capabilities and can also be used to provide anti-piracy and TV rating services. The image tracing technology is used for remote control of personal computers, set-top boxes and televisions as well as gaming consoles.

## Table of Contents

When we license our intellectual property to third parties, we generally receive a combination of license fees and royalties. We mainly license our terminal-end software to the set-top box manufacturers.

We have a non-exclusive license to use the English and Chinese names for NOVEL-TONGFANG and a graphic logo, free of charge, pursuant to an agreement with N-T Information Engineering. N-T Information Engineering has registered these names and the logo as trademarks. Our term of use is from June 1, 2004 until such trademark registrations expire at various dates in 2023. In November 2007, we ceased using NOVEL-TONGFANG in N-S Digital TV's name by changing the name from Beijing Novel-Tongfang Digital TV Technology Co., Ltd. to Beijing Novel-Super Digital TV Technology Co., Ltd. In January 2008, we ceased using the English and Chinese names for NOVEL-TONGFANG as trademarks for our products and we intend not to use such trademarks in the future. We started to use the English and Chinese names for NOVEL SUPERTV in combination with the graphic logo we licensed from N-T Information Engineering as the trademarks for our products. In December 2008, we acquired for free the licensed graphic logo from N-T Information Engineering. In 2010, we completed the registration of the trademarks of the English and Chinese names for NOVEL SUPERTV, as well as the trademark for a combination of Chinese and English names for NOVEL SUPERTV and the graphic logo.

As of December 31, 2012, we owned 60 trademarks 40 of them are registered trademarks and 20 of them are in the process of being registered. We have 35 registered domain names, seven of which were filed with the Ministry of Industry and Information Technology, or MIIT, including novel-supertv.com and chinadtv.cn.

## **Insurance**

We do not maintain any business insurance or key-man insurance. Insurance companies in the PRC offer limited business insurance products and do not, to our knowledge, offer business liability insurance. While business disruption insurance is available to a limited extent in the PRC, we have determined that the risks of disruption, cost of such insurance and the difficulties associated with acquiring such insurance on commercially reasonable terms make it impractical for us to have such insurance. As a result, we do not have any business liability, disruption or litigation insurance coverage for our operations in the PRC. We also generally do not maintain property insurance, except for insurance that covers the company automobiles.

## **Employees**

We had 550, 627 and 778 full-time employees as of December 31, 2010, 2011 and 2012, respectively. We have no part-time employees. Substantially all of our employees are located in the PRC. The table below shows the number of employees categorized by business area and as a percentage of our workforce as of December 31, 2010, 2011 and 2012:

|                            | As of<br>December 31,<br>2010 |        | As of<br>December 31,<br>2011 |        | As of<br>December 31,<br>2012 |        |
|----------------------------|-------------------------------|--------|-------------------------------|--------|-------------------------------|--------|
|                            | Number                        | %      | Number                        | %      | Number                        | %      |
| Research and development   | 308                           | 56.0%  | 334                           | 53.3%  | 439                           | 56.4%  |
| Technical service          | 44                            | 8.0    | 49                            | 7.8    | 58                            | 7.4    |
| Sales and marketing        | 96                            | 17.5   | 148                           | 23.6   | 168                           | 21.6   |
| General and administration | 71                            | 12.9   | 68                            | 10.8   | 83                            | 10.7   |
| Smart card production      | 31                            | 5.6    | 28                            | 4.5    | 30                            | 3.9    |
| Total                      | 550                           | 100.0% | 627                           | 100.0% | 778                           | 100.0% |

As required by applicable PRC regulations, we participate in various employee benefit plans that are organized by municipal and provincial governments, including housing, pension, medical and unemployment benefit plans. We are required under PRC law to make contributions to the employee benefit plans at specified percentages of the salaries, bonuses and certain allowances of our employees, up to a maximum amount specified by the local government from time to time. Members of the retirement plan are entitled to a pension equal to a fixed proportion of the salary prevailing at the member's retirement date. The total contributions made to employee benefit plans in 2010, 2011 and 2012 were approximately US\$2.8 million, US\$3.4 million and US\$5.0 million, respectively.



## **Table of Contents**

Our employees are not represented by any collective bargaining agreements or labor unions. We believe that we maintain a good working relationship with our employees and we have not experienced any significant labor disputes.

We typically enter into a standard confidentiality agreement with our employees. We also enter into an agreement with each of our employees giving us full rights to any inventions developed by such persons during the course of their employment by us. In addition, we enter into a non-competition agreement with each of our executive officers and key research and development personnel. These agreements include a covenant that prohibits each of them from engaging in any activities that directly or indirectly compete with our business during, and for one year after, the period of their employment with us.

## **Regulation**

We operate substantially all of our business in the PRC and various aspects of our business activities are subject to the laws, rules and regulations of the PRC, including laws, rules and regulations relating to the encryption industry, the cable television industry and the software industry. These laws, rules and regulations require us to obtain certain licenses and certificates for our encryption products. In addition, certain laws, rules and regulations of the PRC also affect the rights of our shareholders to receive dividends and other distributions from us. This section summarizes the principal regulations relevant to our lines of business.

### ***Regulation of Encryption Industry***

Encryption software is an essential component of our CA systems. The development, production and sale of commercial encryption products in the PRC is regulated by the PRC National Encryption Administrative Bureau, or the Encryption Bureau, and its authorized local branches. The principal regulations governing the encryption business in the PRC are the *Administrative Regulation for Commercial Cryptogram* promulgated by the State Council in 1999 and a series of rules issued by the Encryption Bureau thereunder.

A company generally is only allowed to produce and/or sell encryption products that have adopted the algorithms designated by the Encryption Bureau and such products shall also be certified by Encryption Bureau. The Encryption Bureau did not initially designate algorithms for CA systems until 2007, and a final and official designation still remains pending. As a result, like many other vendors of CA systems in the PRC, N-S Digital TV has been making and selling CA systems using algorithms other than those initially designated by the Encryption Bureau. Based on our consultation with the Encryption Bureau, we have no reason to believe, given that N-S Digital TV commenced its CA systems business when the initially designated algorithms were not yet available, that the Encryption Bureau would impose any sanctions against N-S Digital TV for not using initially designated algorithms in the past. In addition, since the Encryption Bureau did not initially designate any algorithms for CA systems until 2007 with a final and official designation pending and the CA systems using algorithms other than those initially designated by the Encryption Bureau have been widely used and accepted in the market, the PRC government has allowed vendors of CA systems a transition period, of a duration yet to be determined at its sole discretion, during which such vendors, including N-S Digital TV, may continue to produce and sell CA systems without using government-designated algorithms. The PRC government may require vendors of CA systems to adopt the algorithms to be finally and officially designated by the authority at the expiration of such transition period or at any time during the transition period.

In addition, a company engaging in the encryption-related business is subject to certain licensing requirements. For example, a company engaging in the production of commercial encryption products must obtain a production license from the Encryption Bureau, and a company engaging in the sale and distribution of commercial encryption products must obtain a sales license. In addition, a company engaging in research and development of commercial encryption systems, protocols, algorithms or technical standards shall obtain a license for research and development from the Encryption Bureau. To obtain such licenses, a company must meet requirements established by the Encryption Bureau, among others, with respect to its technological capabilities, its equipment, its production and quality control processes, the level of security of its algorithms and the qualifications of its employees. Furthermore, both importing and exporting products or equipment containing encryption technologies are subject to the prior approval of the Encryption Bureau.

## **Table of Contents**

In the opinion of Han Kun, our PRC counsel, the business of N-S Digital TV does not require a license for research and development. N-S Digital TV has engaged in the production and sale of encryption products since its establishment in May 2004, but it did not obtain the license for the production of encryption products until June 2006, which was renewed in May 2009 and June 2012, and the license for the sale of encryption products until September 2008, which was renewed in September 2011. For risk relating to the potential legal penalties against N-S Digital TV for its operation prior to its obtaining the production and sales licenses, see Item 3. Key Information D. Risk Factors Risk Relating to Our Business and Industry N-S Digital TV may be deemed not to be in full compliance with certain legal regulatory requirements relating to the production, sale and export of encryption products, and the relevant PRC government authorities could require N-S Digital TV to cease such activities and impose administrative penalties including fines, which could have a material adverse effect on our business, financial conditions and results of operations.

Furthermore, the Administrative Regulation for Commercial Cryptogram and the Provisions on the Administration of the Use of Commercial Encryption Products, which became effective in October 1999 and May 2007, respectively, allow users to use only encryption products that are certified by the encryption authority and purchased from vendors who hold an encryption product sales license. Our CA systems that we currently produce and sell have not been certified by the Encryption Bureau because we have not adopted the government-designated algorithms for those CA systems. We believe that because in practice the PRC government has allowed a transition period, of a duration yet to be determined at its sole discretion, for us to adopt the algorithms to be finally and officially designated by the authority, it is unlikely that the government will enforce the above-mentioned regulatory requirements with respect to the use or purchase of our CA systems during that transition period. See also Item 3. Key Information D. Risk Factors Risks Relating to Our Business and Industry Enforcement of recent PRC regulatory requirements regarding the use of encryption products may prevent prospective customers from purchasing our CA systems and our business revenues and net income could be materially reduced as a result.

Although foreign-invested enterprises incorporated in the PRC, such as our subsidiary, Super TV, are not expressly prohibited from conducting encryption-related business, they may have difficulties obtaining the licenses or permits required for conducting such business from the Encryption Bureau due to the Encryption Bureau's generally restrictive approach towards foreign participation in the PRC encryption industry. N-S Digital TV, which is wholly owned by PRC citizens and through which we conduct our CA system business, has obtained the license for the production and sales of commercial encryption products required for our business. Our contractual arrangements with N-S Digital TV and its shareholders provide us with the economic benefits of, and substantive control over, N-S Digital TV. If the Encryption Bureau determines that our control over, or relationship with, N-S Digital TV through those contractual arrangements is contrary to its generally restrictive approach towards foreign participation in the PRC encryption industry, it may reconsider N-S Digital TV's eligibility to hold the license to produce and sell commercial encryption products. The Encryption Bureau may revoke, or refuse to renew, N-S Digital TV's licenses to produce and sell commercial encryption products, or refuse to grant any other encryption-related license that may be required for our business in the future. See Item 3. Key Information D. Risk Factors Risks Relating to Our Corporate Structure The agreements that establish the structure for operating our business may result in the relevant PRC government regulators revoking or refusing to renew N-S Digital TV's licenses for the production and sale of commercial encryption products, or refusing to issue any other license required to engage in an encryption-related business.

### ***Regulation of the Cable Television Industry***

The PRC cable television industry, in which most of our customers operate, is subject to extensive government regulation and control. All PRC cable television network operators are directly or indirectly owned or controlled by provincial or local governments, and their business decisions and strategies are significantly affected by government budgets and spending plans. In April 2005, the PRC State Council issued a notice to allow domestic private investors to invest in PRC companies engaged in the operation and infrastructure development of cable networks, subject to a 49% ownership cap. Foreign ownership of cable television networks and stations, however, is still prohibited.

Cable television network operators are subject to the laws, rules and regulations promulgated from time to time by the State Council, the SARFT and other ministries and government departments. These regulations include the *Administrative Regulations for Television Broadcasting* promulgated by the State Council in 1997, the *Interim Measures regarding the Management of Cable TV* promulgated by a predecessor government agency of the SARFT in 1990 and amended in January 2011, and the *Measures Concerning Network Access Certification of Broadcasting and Television Equipment*, which became effective on August 1, 2004. Under these laws, rules and regulations:

## **Table of Contents**

the establishment of a television station or cable television network requires the approval from the SARFT or its relevant local branch;

the establishment of a digital pay-television channel requires the approval of the SARFT;

basic cable television subscription rates are set by local governments and may not be increased without a public hearing;

cable television networks must be designed, constructed and installed by institutions or companies that meet the qualifications set by the SARFT;

each province and municipality, respectively, can have only one provincial or municipal cable television network; and

various restrictions on television programming must be complied with, including a requirement that television operators shall procure programs only from licensed production companies.

According to the relevant regulations of the SARFT, cable television network operators may not use any network equipment or system unless the SARFT has issued a network access certificate with respect to such equipment or system. In determining whether to issue such a certificate, the SARFT reviews the quality assurance system of the relevant manufacturer or vendor and the results of tests of the equipment or systems. A network access certificate has a term of three years and is subject to annual review by the SARFT or its local branches. N-S Digital TV has obtained network access certificates for our CA systems and SMS products.

According to a policy introduced by the SARFT in 2003 and the Policies to Encourage the Development of Digital TV Industry jointly promulgated by SARFT and other government authorities in January 2008, any cable network operator that uses a non-PRC CA system should use such non-PRC CA system together with a PRC CA system when transmitting broadcasting signals. To satisfy this requirement, a cable network operator that uses a non-PRC CA system must install a parallel PRC CA system. Under these policies, vendors of non-PRC CA systems may sell only to cable network operators that have already installed a PRC CA system or who are willing to purchase a parallel PRC CA system. This may result in a competitive disadvantage for vendors of non-PRC CA systems relative to vendors of PRC CA systems. Such policies do not expressly indicate whether the CA systems produced by a foreign-invested company incorporated in the PRC, such as our subsidiary, Super TV, fall into the category of non-PRC CA systems. In light of this ambiguity, we have established N-S Digital TV, which is wholly owned by PRC citizens, to produce and sell our CA systems. We do not have any equity interest in N-S Digital TV and instead enjoy the economic benefits of, and have substantive control over, N-S Digital TV through contractual arrangements with N-S Digital TV and its shareholders as described in

Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions. There are substantial uncertainties regarding the interpretation and application of the above-described PRC government policies and relevant PRC laws, rules and regulations. Accordingly, the PRC government may determine that N-S Digital TV is a vendor of non-PRC CA systems by virtue of our contractual arrangements with N-S Digital TV and its shareholders. See Item 3. Key Information D. Risk Factors Risks Relating to Our Corporate Structure If the PRC government determines that N-S Digital TV is a vendor of non-PRC CA systems by virtue of the agreements that establish the structure for operating our business, we could face difficulty selling our CA systems in the PRC.

### ***Software Products Registration***

On March 5, 2009, the MIIT issued the *Measures Concerning Software Products Administration*, or Software Measures, which became effective on April 10, 2009 and superseded the prior measures issued in 2000, to regulate software products and promote the development of the software industry in the PRC.

## **Table of Contents**

In order to manufacture software products, a software producer must possess the copyright of such software or have obtained a license from legitimate copyright owner or licensor in connection with such software. Software producers must censor the content of their software products. Software developers or producers are allowed to sell or license their registered software products independently or through agents. Software products developed in the PRC may be registered with the local provincial government authorities in charge of the information industry and filed with the MIIT. If no objection is raised within seven business days from the date of the public announcement made by the MIIT after its receipt of the filing, the software products shall be granted registration certificates. Each registration certificate is valid for five years and may be renewed upon expiration. Registered software products may be qualified for certain tax and other preferential treatments under the industrial policies. The MIIT and other relevant departments may carry out supervision and inspection over the development, production, operation and importing and exporting of software products in the PRC. As of December 31, 2012, we had 38 registered software products.

### ***Tax***

See Item 5. Operating and Financial Review and Prospects A. Operating Results Taxes and Incentives PRC.

### ***Foreign Currency Exchange***

Foreign currency exchange in the PRC is primarily governed by the following regulations:

*Foreign Exchange Administration Rules* (1996), as amended in 2008; and

*Regulations of Settlement, Sale and Payment of Foreign Exchange* (1996).

Under the *Foreign Exchange Administration Rules*, the Renminbi is freely convertible for current account items, including the distribution of dividends, payment of interest, trade and service-related foreign exchange transactions. Conversion of Renminbi for capital account items, such as direct investment, loans, securities investment and repatriation of investment, however, is still generally subject to the approval or verification of the SAFE.

Under the *Regulations of Settlement, Sale and Payment of Foreign Exchange*, foreign-invested enterprises may only buy, sell or remit foreign currencies at those banks authorized to conduct foreign exchange business after providing valid commercial documents and, in the case of capital account item transactions, obtaining approval from the SAFE. Capital investments by foreign-invested enterprises outside of the PRC are also subject to limitations, which include approvals by the MOFCOM, the SAFE and the National Development and Reform Commission.

### ***Stock Incentive Plans***

On December 25, 2006, the People's Bank of China issued the Administrative Measures on Individual Foreign Exchange Control, and on January 5, 2007, the SAFE issued the Implementation Rules of the Administrative Measures on Individual Foreign Exchange Control, both of which became effective on February 1, 2007. Under these regulations, all foreign exchange matters involved in employee share ownership plans, share option plans and other equity incentive plans participated by PRC individuals are to be transacted upon the approval from the SAFE or its authorized branches.

On February 15, 2012, the SAFE promulgated SAFE Notice 7, which superseded SAFE Notice 78. Under SAFE Notice 7, Domestic Individuals who are granted stock options or any other stock-related rights and benefits under a stock incentive plan by an overseas-listed company are required, through a Domestic Agent, to register with the SAFE or its authorized local counterparts and complete certain other procedures. The Domestic Agent is required to submit information relating to a stock incentive plan with the authorized local counterparts of the SAFE within three business days of each quarter and complete foreign exchange cancellation procedures within 20 business days after the termination of a stock incentive plan.

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## **Table of Contents**

### ***Dividend Distribution***

The principal regulations governing distribution of dividends paid by wholly foreign-owned enterprises include:

*Wholly Foreign-Owned Enterprise Law* (1986), as amended in 2000; and

*Wholly Foreign-Owned Enterprise Law Implementation Rules* (1990), as amended in 2001.

Under these regulations, wholly foreign-owned enterprises in the PRC may pay dividends only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. In addition, according to the *PRC Company Law*, wholly foreign-owned enterprises in the PRC, like other PRC companies, are required to set aside to fund a statutory reserve each year at least 10% of their after-tax profit, based on PRC accounting standards, until the cumulative total of such reserve reaches 50% of its registered capital. This reserve is not distributable as cash dividends to equity owners.

### ***Regulation of Foreign Exchange in Certain Onshore and Offshore Transactions***

In October 2005, the SAFE issued SAFE Notice 75, which became effective as of November 1, 2005, and was further supplemented by a series of implementation rules and guidances. The SAFE regulations provide that PRC residents, whether natural or legal persons, must register with the relevant local SAFE branch in connection with establishing or taking control of an offshore entity established for the purpose of overseas equity financing involving onshore assets or equity interests held by them. The term “PRC legal person residents” as used in the SAFE regulations refers to those entities with legal person status or other economic organizations established within the territory of the PRC. The term “PRC natural person residents” as used in the SAFE regulations includes all PRC citizens and all other natural persons, including foreigners, who habitually reside in the PRC for economic benefit.

PRC residents are required to complete amended registrations with the local SAFE branch upon: (1) injection of equity interests or assets of an onshore enterprise to the offshore entity; or (2) subsequent overseas equity financing by such offshore entity. PRC residents are also required to complete amended registrations or filing with the local SAFE branch after any material change in the shareholding or capital of the offshore entity, such as changes in share capital, share transfers, long-term equity or debt investments, provision of security and any other material change in the offshore entity. PRC residents who have already incorporated or gained control of offshore entities that have made onshore investment in the PRC before SAFE Notice 75 was promulgated must register their shareholding in the offshore entities with the local SAFE branch on or before March 31, 2006.

Under the SAFE regulations, PRC residents are further required to repatriate into the PRC all of their dividends, profits or capital gains obtained from their shareholdings in the offshore entity within 180 days of their receipt of such dividends, profits or capital gains. The registration and filing procedures under the SAFE regulations are prerequisites for other approval and registration procedures necessary for capital inflow from the offshore entity, such as inbound investments or shareholders loans, or capital outflow to the offshore entity, such as the payment of profits or dividends, liquidating distributions, equity sale proceeds, or the return of funds upon a capital reduction.

### ***Regulation of Overseas Listings***

On August 8, 2006, six PRC regulatory agencies, including the MOFCOM, the State Administration of State-owned Assets Supervision and Administration Commission, the SAT, the State Administration for Industry and Commerce, the CSRC and the SAFE, jointly adopted the M&A Rules, which became effective on September 8, 2006 and was amended on June 22, 2009. The M&A Rules, among other things, include provisions that purport to require that an offshore special purpose vehicle formed for the purpose of an overseas listing of securities in a PRC company and controlled directly or indirectly by PRC companies or individuals obtain the approval of the CSRC prior to the listing and trading of such special purpose vehicle’s securities on an overseas stock exchange.

We completed the initial listing and trading of our ADSs on the NYSE on October 11, 2007. We did not seek CSRC approval in connection with our initial public offering, as we were advised by our PRC counsel that, based on their understanding of the current PRC laws, regulations and rules, because we completed our restructuring before September 8, 2006, the effective date of the M&A Rules, we were not required by the M&A Rules to apply to the CSRC for approval of the listing and trading of our ADSs on a U.S. stock exchange, unless we were clearly required to do so by any rules promulgated in the future. See Item 3. Key Information D. Risk Factors Risks Relating to the People’s Republic of China The approval of the CSRC, might be required in connection with our initial public offering under certain PRC regulation; failure to obtain this approval, if required, could have a material adverse effect on our business, financial conditions, results of operations and reputation as well as

the trading price of our ADSs.

**Table of Contents**

**C. Organizational Structure**

We are a Cayman Islands holding company and conduct substantially all of our business through Super TV, our operating subsidiary in the PRC, and through N-S Digital TV, a PRC company that we control through contractual arrangements. We own 100% of the equity interest of CDTV BVI, a BVI holding company, that directly owns 100% of the equity interest of Golden Benefit and China Super Media Holdings Limited, or CSM Holdings, each a Hong Kong holding company. Golden Benefit, in turn, directly owns 100% of the equity interest of Super TV. In order to assure that the PRC government does not deem our CA systems to be non-PRC CA systems, which would result in a significant competitive disadvantage for us in the PRC market, we have established N-S Digital TV, which is wholly owned by PRC citizens, to produce and sell our CA systems in the PRC. We do not have any equity interest in N-S Digital TV, but instead enjoy the economic benefits derived from N-S Digital TV through a series of contractual arrangements.

The following diagram illustrates our corporate structure as of the date of this annual report:

**Table of Contents**

- (1) Wenjun Wang, Tianxing Wang, Shizhou Shen and Lei Zhang are our employees.
  - (2) Two of our directors, Dr. Zengxiang Lu and Jianhua Zhu, are also directors of N-S Digital TV.
- N-T Information Engineering was established by Tsinghua Enterprise Group, a company affiliated with Tsinghua University, and Hong Kong-based Tsinghua Novel Hi-Tech Investment Holding Ltd. in July 1998, and initially focused on developing, producing and selling digital data broadcasting equipment for cable television operators. In December 2002, N-T Information Engineering completed its acquisition of the CA systems-related assets of Tsinghua Tongfang. In March 2004, CDTV BVI was incorporated as a holding company in the BVI. Following the establishment of CDTV BVI, we restructured our operations in connection with an investment by SAIF. As part of this restructuring, we established Super TV, a wholly-owned subsidiary of CDTV BVI, on May 31, 2004. On the same day, N-S Digital TV was also established. In June 2004, N-S Digital TV acquired from N-T Information Engineering its smart card and CA systems business and, in August 2006, N-S Digital TV acquired from N-T Information Engineering its set-top box design business. In April 2007, a new holding company, CDTV Holding, was established in the Cayman Islands. In May 2007, CDTV BVI executed a 40-for-1 share split of its ordinary shares and Series A preferred shares. Following this share split, the shareholders of CDTV BVI exchanged all of their shares of CDTV BVI for shares of CDTV Holding in proportion to their percentage interest in CDTV BVI. As a result, CDTV BVI became a wholly-owned subsidiary of CDTV Holding. As a result of a series of transactions over the years, Tianxing Wang, Lei Zhang, Shizhou Shen and Wenjun Wang in aggregate own all of the equity interest of N-S Digital TV.

**Table of Contents**

In order to benefit from the tax arrangement between the PRC and Hong Kong, in December 2007, CDTV BVI acquired Golden Benefit, a company incorporated in Hong Kong, for a nominal consideration, and transferred its 100% equity interest in Super TV to Golden Benefit. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China We may be subject to PRC income tax on our global income, or dividends we receive from our PRC subsidiary may be subject to PRC withholding tax, depending on whether we are recognized as a resident enterprise in the PRC and Item 5. Operating and Financial Review and Prospects A. Operating Results Taxes and Incentives Tax Arrangement between PRC and Hong Kong.

In December 2007, Super TV established a wholly-owned subsidiary, N-S Media Investment, in the PRC to partner with the PRC's cable television operators and content providers to offer value-added services to television viewers. In light of the applicable PRC regulatory restrictions on foreign investment in advertising business, which some of the value-added television services to be offered by N-S Media Investment and its subsidiaries could be categorized as, Super TV transferred all of its equity interests in N-S Media Investment to N-S Digital TV in October 2008. In February 2008, CDTV BVI established a wholly-owned subsidiary, CSM Holdings, in Hong Kong. In addition, in June 2008, N-S Digital TV established a joint venture, Dongguan SuperTV, with other investors to provide value-added services to television viewers in Dongguan, Guangdong Province. In September 2008, N-S Digital TV exercised an option to purchase an additional 10% equity interest in the joint venture from Mr. Lai. In July 2009, N-S Digital TV sold its 20% equity interest in Dongguan SuperTV to a new investor, Guangdong Jiakai. In August 2010, N-S Digital TV entered into an equity transfer agreement with Guangdong Jiakai to repurchase the 20% equity interest in Dongguan SuperTV from Guangdong Jiakai. After these transactions, the equity interest of Dongguan SuperTV held by N-S Digital TV increased to 60% and N-S Digital TV became entitled to 70% of shareholders' voting rights in Dongguan SuperTV. In December 2011, N-S Digital TV sold its entire equity interest in Dongguan SuperTV to a third party. In October 2008, N-S Media Investment established a wholly-owned subsidiary, Guangdong SuperTV, to provide value-added services to television viewers in Guangdong Province. In August 2010, all of the equity interest in Guangdong SuperTV was transferred to Guangzhou Rujia.

In April 2010, we established N-S Digital Technology, a wholly-owned subsidiary of Golden Benefit, in the PRC. In March 2011, N-S Digital Technology was dissolved. In July 2010, we established N-S Investment Holdings, a wholly-owned subsidiary of Super TV, in the PRC. In addition, in January 2011, we established Cyber Cloud, a subsidiary in which Super TV holds a 90% equity interest, in the PRC. In May 2011, we established Joysee, a subsidiary in the PRC in which Super TV and N-S Digital TV hold 46.9% and 17.9% equity interest, respectively. In September 2011, we established Super Movie, a subsidiary in the PRC in which Super TV holds a 90% equity interest.

Any cable network operator who uses a non-PRC CA system is required under a policy promulgated by the SARFT to install a parallel PRC CA system. Under this policy, vendors of non-PRC CA systems may sell only to cable network operators who have already installed a PRC CA system or are willing to purchase a parallel PRC CA system. This may result in a competitive disadvantage for vendors of non-PRC CA systems relative to vendors of PRC CA systems. Such policy does not expressly indicate whether the CA systems produced by a foreign-invested company incorporated in the PRC, such as our subsidiary Super TV, falls into the category of non-PRC CA systems. In light of this ambiguity, we have established N-S Digital TV, which is incorporated in the PRC and wholly owned by PRC citizens, to produce and sell our CA systems to avoid our CA systems being deemed as non-PRC CA systems. We conduct a significant portion of our operations through N-S Digital TV. We do not directly or indirectly have any equity interest in N-S Digital TV, but Super TV, our wholly-owned subsidiary in the PRC, has entered into a series of contractual arrangements with N-S Digital TV and its shareholders. As a result of these contractual arrangements, we are considered the primary beneficiary of N-S Digital TV and, accordingly, we consolidate N-S Digital TV's results of operations in our financial statements.

Super TV mainly engages in supplying software products relating to smart cards to N-S Digital TV, providing technical support and related services to N-S Digital TV, and developing technology for use by N-S Digital TV. Specifically, Super TV and N-S Digital TV have entered into the following contracts:

a products and software purchase agreement, pursuant to which N-S Digital TV purchased from Super TV all software products relating to smart cards required for N-S Digital TV's CA systems;

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**Table of Contents**

a technical support and related services agreement, pursuant to which Super TV exclusively provides N-S Digital TV and/or its customers with technical support, technical training, personnel services in connection with N-S Digital TV's marketing activities and services relating to the maintenance and optimization for the products and software of N-S Digital TV's customers at N-S Digital TV's request;

a technology license agreement, pursuant to which N-S Digital TV grants Super TV, free of charge, an exclusive license to use certain software copyrights, patents, unpatentable technologies and technical secrets relating to the digital television business that was transferred from N-T Information Engineering to N-S Digital TV; and

a technology development agreement, pursuant to which N-S Digital TV engages Super TV to develop all technology required by N-S Digital TV or its customers.

In addition, Super TV has entered into the following agreements with N-S Digital TV and its shareholders that provide us with the ability to control N-S Digital TV:

Equity Transfer Option Agreement, pursuant to which the shareholders of N-S Digital TV have jointly granted Super TV or its designated party an exclusive and irrevocable option to purchase all of their equity interests in N-S Digital TV at any time, and, without Super TV's prior written consent, the shareholders of N-S Digital TV may not: (1) transfer or pledge their equity interests in N-S Digital TV; (2) cause N-S Digital TV to issue new shares; (3) receive any dividends, loan interest or other benefits from N-S Digital TV; or (4) make any material adjustment or change to N-S Digital TV's business or operations;

Business Operating Agreement, pursuant to which N-S Digital TV and its shareholders agreed to: (1) accept the policies and guidelines furnished by Super TV with respect to the hiring and dismissal of employees, the operational management and financial system of N-S Digital TV; (2) appoint the candidates recommended by Super TV as directors of N-S Digital TV and appoint the senior management personnel of Super TV as the general manager, chief financial officer and other senior officers of N-S Digital TV based on Super TV's recommendations; (3) replace or remove a director or senior management personnel of N-S Digital TV upon Super TV's request; and (4) seek a guarantee from Super TV first when any guarantee is required to secure performance by N-S Digital TV of any contract or working capital loans borrowed by N-S Digital TV;

loan agreements, pursuant to which each shareholder of N-S Digital TV has obtained loans from Super TV to fund its contribution to N-S Digital TV's registered capital and has agreed to: (1) not repay the loan prior to the termination date of the relevant loan agreement, unless so requested by Super TV; and (2) only repay the loan by (i) transferring all his equity interests in N-S Digital TV to Super TV or any third party designated by Super TV and (ii) paying Super TV with the entire proceeds obtained by himself from such transfer;

powers of attorney, pursuant to which each shareholder of N-S Digital TV has irrevocably appointed Super TV or one of its directors as their attorneys-in-fact to exercise all its voting rights as shareholders of N-S Digital TV; and

share pledge agreements, pursuant to which each shareholder of N-S Digital TV has pledged all of its respective equity interests in N-S Digital TV to Super TV to secure the performance of its and N-S Digital TV's obligations under certain contractual arrangements between N-S Digital TV and/or its shareholders and Super TV.

For a more detailed description of these contractual agreements, see Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Super TV and N-S Digital TV Arrangements and Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Shareholder Rights and Corporate Governance.

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## **Table of Contents**

### **D. Property, Plants and Equipment**

We currently maintain our headquarters and most of our operations at Jingmeng High-Tech Building B, 4th Floor, No. 5 Shangdi East Road, Haidian District, Beijing 100085, PRC, where we lease 8,616 square meters of office space pursuant to four short-term lease agreements with the same landlord for separate portions of the total space. The four lease agreements are: (1) a lease agreement of N-S Digital TV with respect to an aggregate area of 2,185 square meters for its operational use; (2) a lease agreement of Super TV with respect to an aggregate area of 4,828 square meters for its operational use and an aggregate area of 180 square meters for storage; (3) a lease agreement of Joysee with respect to an area of 1,130 square meters for its operational use; and (4) a lease agreement of Super Movie with respect to an aggregate area of 293 square meters for its operational use. All the lease agreements expired in April 2013. We intend to continue leasing the forgoing space and are currently in the process of finalizing the relevant leasing arrangements with the landlord. We also maintain the operations of Cyber Cloud at Deshi Building, 5th Floor, No. 9 Shangdi East Road, Haidian District, Beijing 100085 PRC, where we have leased 2,050 square meters of office space pursuant to a two-year lease agreement which will expire in July 2014.

In addition, we lease office space for service and support centers in Hangzhou and Nanhai. We routinely review our needs for office space in light of the development of our operations. We believe that the office space that we currently lease is sufficient for our current and immediately foreseeable needs. We may lease additional space if needed in the future.

### **Item 4A. Unresolved Staff Comments**

None.

### **Item 5. Operating and Financial Review and Prospects**

The following discussion and analysis should be read in conjunction with our consolidated financial statements and the related notes included elsewhere in this annual report. Our audited consolidated financial statements have been prepared in accordance with U.S. GAAP. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those projected in the forward-looking statements. In evaluating our business, you should carefully consider the information provided in Item 3. Key Information D. Risk Factors.

#### **A. Operating Results**

##### **Overview**

We are the leading provider of CA systems to the PRC digital television market. Our CA systems, which consist of smart cards, head-end software for television network operators and terminal-end software for set-top box manufacturers, enable digital television network operators in the PRC to control the distribution of content and value-added services to their subscribers and block unauthorized access to their networks. In addition, we sell advanced digital television application software, such as electronic program guides and subscriber management systems, to digital television network operators.

We sell our CA systems and digital television application software to PRC television network operators, including cable, satellite and terrestrial television network operators and enterprises that maintain private cable television networks within their facilities. We currently derive, and we expect to continue to derive, a significant portion of our revenues during any given period from a limited number of customers, primarily cable television network operators who are launching new digital transmission systems, although the particular customers may vary from period to period.

PRC television network operators are in the process of migrating from analog to digital transmissions, and the PRC government has set a target of 2015 for cable operators nationwide to complete the digital transition. As of December 31, 2012, we had installed CA systems at 385 digital television network operators in 29 of the 32 provinces, autonomous regions and centrally administered municipalities in the PRC. We have also been installing CA systems outside the PRC since 2010. We derive a substantial majority of our revenues from sales of our smart cards, which accounted for 93.6%, 91.5% and 83.3% of our total revenues in 2010, 2011 and 2012, respectively. We expect that sales of our smart cards will continue to constitute the majority of our revenues in the near future. We sold 16.2 million, 18.3 million and 15.3 million smart cards in 2010, 2011 and 2012, respectively, and our net revenues were US\$87.1 million, US\$99.1 million and US\$88.7 million in 2010, 2011 and 2012, respectively. Our net income was US\$33.4 million, US\$40.3 million and US\$5.5 million in 2010, 2011 and 2012, respectively.



## **Table of Contents**

Among the most significant factors affecting our business, financial condition and results of operations are:

***Progress of continued digitalization and growth of digital television network operators' subscriber base in the PRC.*** Our continued success depends on the pace at which PRC television network operators continue to switch from analog to digital transmission as well as further growth in our customers' subscriber base. If the PRC government postpones its target date for digitalization, or our customers fail to roll out analog-to-digital conversion or attract subscribers to digital television, we may be unable to sustain or grow our revenues.

***Pricing.*** The business in which we operate is subject to intense competition, particularly with respect to pricing of our products and services. Our customers generally expect to receive volume-based discounts from us, and we may be required to reduce prices for large purchases or if competition intensifies.

***Purchasing patterns of our customers.*** Our customers generally purchase smart cards from us based on the number of digital television subscribers they expect to add in the immediate near term, resulting in significant fluctuations in our revenues from period to period due to the uncertainty of both the timing and the amount of such customer orders.

***Ability to respond effectively to technological and commercial changes.*** Our business and the market in which we operate are characterized by rapid commercial and technological change, evolving industry standards and frequent product enhancements. Our continued success will depend, in part, on our ability to continue developing and marketing products and services that respond to technological changes and evolving market demand or industry standards in a timely and cost-effective manner.

***Cost structure.*** Our profitability also depends on the cost structure of our operations, including, among other things, the costs of computer chips sourced from third-party suppliers and personnel costs.

In addition to the factors discussed above, our reported results are also affected by the fluctuations in the value of the Renminbi against the U.S. dollar, as our reporting currency is the U.S. dollar while the functional currency of our subsidiaries and variable interest entities in China, which operate substantially all of our business, is the Renminbi. In 2010, 2011 and 2012, the Renminbi appreciated against the U.S. dollar by approximately 3.3%, 4.6% and 1.0%, respectively. The appreciation of the Renminbi against the U.S. dollar contributed to the increase in our net income reported in U.S. dollar terms in 2010, 2011 and 2012, respectively. For additional information relating to the fluctuations in the value of the Renminbi against the U.S. dollar, see Item 3. Key Information A. Selected Financial Data Exchange Rate Information, Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China Fluctuations in exchange rates could result in foreign currency exchange losses. and Item 11. Quantitative and Qualitative Disclosures About Market Risks Foreign Currency Risk.

Our business is managed as a single operating segment. Our management reviews our consolidated results of operations prepared in accordance with U.S. GAAP when making decisions about allocating our resources and assessing our performance.

## **Revenues**

We derive revenues primarily from the following two sources:

## **Table of Contents**

**Products.** We currently derive a substantial majority of our revenues from sales of smart cards and other products to digital television network operators. Smart cards are an essential part of our CA systems. Our customers purchase our smart cards for distribution to and use by their subscribers in their set-top boxes. Revenues from the sales of our smart cards account for substantially all of our revenues from the sales of our products. In addition, we also sell small quantities of other products, such as integrated chips, surface mounted device chips and multimedia home entertainment boxes. We expect that the sales of our smart cards will continue to constitute the majority of our revenues in the near future.

**Services.** We derive revenues from providing head-end system integration services and head-end system development services to digital television network operators, collecting licensing fees and/or royalty income from set-top box manufacturers and digital television operators. Our head-end system integration services involve providing head-end software, hardware and related system integration services to our customers. Head-end software mainly consists of software for CA systems, subscriber management systems and electronic program guides. Our head-end system development services involve the development of customized digital television-related software applications for our customers. In addition, we provide set-top box manufacturers with our CA system terminal-end software that enables them to manufacture set-top boxes compatible with our CA systems, and receive one-time licensing fees as well as royalties from such set-top box manufacturers.

In certain circumstances, we receive royalties from digital television network operators who purchase smart cards for use with set-top boxes that were manufactured using our CA system terminal-end software, in lieu of collecting royalties from the relevant set-top boxes manufacturers. We include such royalty income as part of the revenue from sales of the related smart cards.

Revenues from the sales of our products and services accounted for 94.5% and 5.5%, respectively, of our total revenues in 2012 compared to 94.7% and 5.3%, respectively, of our total revenues in 2011. Our revenues also include certain refunds of value-added taxes from PRC tax authorities that we previously paid with respect to some of our software products. See Item 5. Operating and Financial Review and Prospects A. Operating Results Taxes and Incentives below for more information.

Our net revenues represent total revenues less PRC business tax and related surcharges. See Item 5. Operating and Financial Review and Prospects A. Operating Results Taxes and Incentives PRC Business Tax below for more information.

### **Cost of Revenues**

Cost of revenues primarily includes: costs of raw materials, such as computer chips manufactured by third-party suppliers and used in our smart cards and other products; personnel costs directly relating to provision of our services; warranty costs relating to our smart card sales; depreciation and amortization costs; share-based compensation allocated to the production and processing of our smart cards and other products; fees paid to our sales agents; and other miscellaneous costs. These costs are allocated to our two types of revenue-generating activities as their respective costs of revenues. Cost of revenues related to the sales of our products and to the sales of our services accounted for 81.0% and 19.0%, respectively, of our total cost of revenues in 2012 compared to 84.2% and 15.8%, respectively, of our total cost of revenues in 2011. As a percentage of our net revenues, cost of revenues increased from 19.3% in 2011 to 23.5% in 2012.

### **Gross Profit and Gross Margin**

Gross profit is equal to net revenues less cost of revenues. Gross margin is equal to gross profit divided by net revenues. Our gross margin was 79.1%, 80.7% and 76.5% in 2010, 2011 and 2012, respectively. The increase in our gross margin from 2010 to 2011 was primarily attributable to changes in product mix, reflecting an improvement in our higher margin businesses, principally from sales of smart cards, as well as decreases in the unit cost of smart cards. The decrease in our gross margin from 2011 to 2012 was mainly due to a decrease in our smart cards sales coupled with an increase in sales of other products, which have lower gross margins than smart cards.

The average unit cost of our smart cards in U.S. dollar terms decreased by approximately 10.0% from 2010 to 2011 and further decreased by approximately 0.4% from 2011 to 2012, principally as a result of the continuing decline in chip and production costs.

## Table of Contents

### Operating Expenses

Our operating expenses consist of research and development expenses, selling and marketing expenses and general and administrative expenses. Each of these components of our operating expenses includes a portion of our total share-based compensation expenses, which are generally allocated according to the functions of those individuals who received share-based awards.

**Research and Development Expenses.** Research and development expenses consist primarily of costs associated with the design, development and testing of our products and technologies. Among other things, these costs include compensation and benefits for our research and development staff, rental for our office premises used for research and development activities, depreciation expenses related to equipment used in research and development activities, expenditures for purchases of supplies and other relevant costs. Compensation and benefits for our research and development staff accounted for the majority of our research and development expenses. Research and development expenses as a percentage of our net revenues were 13.3% and 19.6% in 2011 and 2012, respectively.

**Selling and Marketing Expenses.** Selling and marketing expenses consist primarily of compensation and benefits for our sales and marketing staff, expenses for promotional, advertising, travel and entertainment activities, marketing-related consulting fees, expenditures for purchases of supplies and amortization of intangible assets. Selling and marketing expenses as a percentage of our net revenues were 12.5% and 15.3% in 2011 and 2012, respectively.

**General and Administrative Expenses.** General and administrative expenses consist primarily of compensation and benefits for our general management, finance and administrative staff, professional advisory fees, depreciation and amortization with respect to equipment used for general corporate purposes, rental costs for our office premises used by general management, finance and administrative staff, and other expenses incurred in connection with general corporate purposes. General and administrative expenses as a percentage of our net revenues were 9.8% and 10.6% in 2011 and 2012, respectively.

**Share-Based Compensation Expenses.** We account for share-based compensation expenses based on the fair value of share option grants at the date of grant.

We adopted our 2005, 2008, 2010 and 2012 Stock Incentive Plans in February 2005, September 2007, November 2010 and May 2012, respectively, and options to purchase an aggregate of 5,303,941 ordinary shares have been granted and were outstanding under the plans as of March 31, 2013. In January 2013, we granted options to purchase 1,200,000 ordinary shares to 101 of our employees, including options to purchase 150,000, 150,000, 38,000, 32,000, 26,000, and 50,000 ordinary shares to Jianhua Zhu, our chairman and chief executive officer, Zengxiang Lu, a member of our board of directors, Zhenwen Liang, our chief financial officer, Dong Li, our president and chief marketing officer, Huiqing Chen, our chief administrative officer, and Tianxing Wang, our chief technology officer, respectively. We incurred share-based compensation expenses of US\$1.5 million, US\$5.6 million and US\$2.6 million in 2010, 2011 and 2012, respectively. For additional information regarding our share-based compensation expenses, see Note 20 to our consolidated financial statements included elsewhere in this annual report.

The table below shows the allocation of share-based compensation charges to cost of revenues and our operating expense line items for the periods indicated:

| Share-Based Compensation Related to: | For the years ended December 31, |                   |                   |
|--------------------------------------|----------------------------------|-------------------|-------------------|
|                                      | 2010                             | 2011              | 2012              |
|                                      | (In thousands)                   |                   |                   |
| Cost of revenues                     | US\$ 10                          | US\$ 52           | US\$ 5            |
| Research and development expenses    | 393                              | 1,025             | 552               |
| Selling and marketing expenses       | 384                              | 633               | 356               |
| General and administrative expenses  | 691                              | 3,852             | 1,701             |
| <b>Total</b>                         | <b>US\$ 1,478</b>                | <b>US\$ 5,562</b> | <b>US\$ 2,614</b> |

## **Table of Contents**

### **Income from Operations**

Income from operations represents gross profit less operating expenses.

### **Non-operating Income/(Expenses)**

Non-operating income/(expenses) includes interest income/(expense), gain from foreign currency forward contracts, impairment loss on long-term investments and other income/(expense), each as presented in our consolidated statements of comprehensive income. Our interest income was US\$5.3 million, US\$6.8 million and US\$6.3 million in 2010, 2011 and 2012, respectively. We had interest expense of US\$1.5 million and US\$0.7 million in 2011 and 2012, respectively. We recorded a gain from foreign currency forward contracts, which were entered into in April and May 2011, of US\$0.4 million in 2011 and a loss from foreign currency forward contracts of US\$0.7 million in 2012. Our impairment loss on long-term investments was US\$5.0 million, nil and US\$4.5 million in 2010, 2011 and 2012, respectively. We also had other expense of US\$0.09 million in 2010 and other income of US\$0.6 million and US\$0.5 million in 2011 and 2012, respectively.

### **Corporate Structure**

We are a Cayman Islands holding company and conduct substantially all of our business through Super TV, our indirectly wholly-owned subsidiary in the PRC. In May 2004, we established N-S Digital TV, a PRC company that is wholly owned by PRC citizens, to carry out our CA systems business in the PRC. We do not directly or indirectly have any equity interest in N-S Digital TV, but Super TV has entered into a series of contractual arrangements with N-S Digital TV and its shareholders. As a result of these contractual arrangements, we have the power to direct the activities that most significantly affects the economic performance of N-S Digital TV and its subsidiaries and to receive the economic benefits of these entities that could be significant to them. As a result, we are considered the primary beneficiary of N-S Digital TV and we consolidate N-S Digital TV's results of operations in our financial statements. For a description of these contractual agreements, see Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Super TV and N-S Digital TV Arrangements and Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions Shareholder Rights and Corporate Governance.

### **Critical Accounting Policies**

We prepare our financial statements in conformity with U.S. GAAP, which requires us to make estimates and assumptions that affect our reporting of, among other things, assets and liabilities, contingent assets and liabilities and revenues and expenses. We continually evaluate these estimates and assumptions based on the most recently available information, our own historical experiences and other factors that we believe to be relevant under the circumstances. Since our financial reporting process inherently relies on the use of estimates and assumptions, our actual results could differ from what we expect. This is especially true with some accounting policies that require higher degrees of judgment than others in their application. We consider the policies discussed below to be critical to an understanding of our consolidated financial statements because they involve the greatest reliance on our management's judgment.

## **Table of Contents**

**Revenue Recognition.** We derive revenues primarily from two sources: (1) sales of products, including smart cards and other products sourced from third-party suppliers, such as integrated chips, surface mounted device chips and multimedia home entertainment boxes; and (2) provision of services, including head-end system integration services, head-end system development services and CA system terminal-end software that generate licensing income and royalty income.

For sales of our products, we recognize revenue when the products are delivered to and received by customers.

Our head-end integration services primarily involve provision of our head-end software, third-party hardware and software, related installation and integration services, training and post-contract customer support, or PCS, including telephone support and bug-fixing. Our head-end system development services involve the development of customized digital television technology-related software applications. Head-end software offered by us includes CA systems head-end software, SMS software and electronic program guide software.

We sign head-end system integration contracts with cable television network operators to install and integrate our software with third-party hardware and software. Once the service is substantially completed, customers will issue a preliminary acceptance, while a final acceptance is usually issued six months to one year after the issuance of preliminary acceptance if no major technical problems are discovered. In the majority of our head-end system integration contracts, we offer free PCS for one year, beginning from preliminary acceptance by customers. Based on historical information, we believe that a final acceptance is not a significant event because essentially all the services we were obligated to provide have been delivered and all technical problems, if any, have been detected at the point of the preliminary acceptance by the customer and the cost of additional work between a preliminary acceptance and a final acceptance has historically been insignificant.

With respect to the contracts in which we offer free PCS for one year or less, we recognize revenue when all installation and integration services are completed, which is generally indicated by obtaining the preliminary acceptances from customers. With respect to contracts in which we offer free PCS for more than one year, although the costs incurred during the PCS term have historically been insignificant, we defer the revenue and ratably recognize it over the PCS term. Where we offer PCS for an unspecified period, we ratably recognize the relevant revenue over the estimated useful life of our CA systems, which we determined to be five years.

With respect to our head-end system development services, we use the completed-contract method to recognize revenue when the software application development is finished and accepted by customers, as we currently do not have a reliable mechanism to measure the progress toward completion of the service.

We receive licensing fees from set-top box manufacturers who license our CA systems terminal-end software, and we are also entitled to receive royalties from them based on the quantity of set-top boxes manufactured under such licenses. Royalty income is recognized upon receipt of sales reports from the set-top box manufacturers and when payment is received, while licensing income is recognized upon the issuance of certificates to the set-top box manufacturers by us.

**Deferred Costs.** Where revenue from a head-end system integration contract is deferred and recognized over the PCS term, we defer the costs directly associated with such revenue. Such costs mainly relate to hardware and software purchased from third-party suppliers. Deferred costs are recorded as an asset and amortized to cost of revenue over the same period as that over which the corresponding revenue is recognized.

**Goodwill.** The excess of the purchase price over the fair value of net assets acquired is recorded on the consolidated balance sheet as goodwill. Goodwill is not amortized but tested for impairment on an annual basis and between annual tests if an event or circumstance would more likely than not reduce the fair value of a reporting unit below its carrying value. Such an event or circumstance includes a significant change in the 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

The 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. Estimating fair value is performed by utilizing various valuation techniques, with the primary technique being a discounted cash flow analysis. Discounted cash flow analysis requires significant judgments, including the estimation of future cash flows, which is dependent on internal forecasts, the estimation of long term growth rate of a company's business, the estimation of the useful life over which cash flows will occur, and the determination of a company's weighted average cost of capital.

In 2012, we adopted an accounting pronouncement, issued by the Financial Accounting Standards Board in September 2011, which permits us to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. If it is more likely than not that the fair value of a reporting unit is less than its carrying amount, goodwill is then tested following a two-step process. The first step compares the fair value of a reporting unit to its carrying amount, including goodwill. If the fair value of the reporting unit is greater than its carrying amount, goodwill is not considered impaired and the second step is not required. If the fair value of the reporting unit is less than its carrying amount, the second step of the impairment test measures the amount of the impairment loss, if any, by comparing the implied fair value of goodwill to its carrying amount. If the carrying amount of goodwill exceeds its implied fair value, an impairment loss is recognized equal to that excess. The implied fair value of goodwill is calculated in the same manner that goodwill is calculated in a business combination, whereby the fair value of the reporting unit is allocated to all of the assets and liabilities of that unit, with the excess purchase price over the amounts assigned to assets and liability representing the implied fair value of goodwill. We have one reporting unit and have determined to perform the annual impairment test on December 31 of each year. In 2012, we first assessed the qualitative factors to determine whether it is not more likely than not that the fair value of the reporting unit is less than its carrying amount. We did not incur any impairment loss on goodwill for the years ended December 31, 2010, 2011 and 2012.

**Impairment of Long-Lived Asset.** We review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may no longer be recoverable. When these events occur, we measure impairment by comparing the carrying value of the long-lived assets to the estimated undiscounted future cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected undiscounted cash flows is less than the carrying amount of the assets, we would recognize an impairment loss based on the fair value of the assets. Impairment loss in 2010, 2011 and 2012 was US\$20,000, nil and nil, respectively.

**Equity Method Investments.** Investee companies over which we have the ability to exercise significant influence, but do not have a controlling interest, are accounted for using the equity method. Significant influence is generally considered to exist when we have an ownership interest in the voting stock of the investee between 20% and 50%, and other factors, such as representation on the investee's board of directors, voting rights and the impact of commercial arrangements, are considered in determining whether the equity method of accounting is appropriate.

Investee companies over which we have equity interest over 50%, but where the noncontrolling shareholders have substantive rights to participate in significant operating decisions, are accounted for using the equity method.

An impairment charge is recorded if the carrying amount of the investment exceeds its fair value and this condition is determined to be other-than-temporary. We accrued a full impairment charge of US\$4.5 million in 2012 related to our investment in 3DiJoy based on the fair value of 3DiJoy we estimated with the assistance of a third party valuation firm, as we had doubts regarding 3DiJoy's ability to operate as a going concern given that it had been experiencing financial difficulties and had failed to obtain new capital funding from its shareholders or otherwise. Our equity method investment in 3DiJoy is considered as Level 3 assets because we used unobservable inputs, such as weighted average cost of capital, or WACC, and lack of marketability discount, or LoMD, to determine the fair value of such equity method investment. The WACC and LoMD used in the fair value measurement were 22% and 40%, respectively. Increase (or decrease) in any of the WACC and LoMD in isolation may result in a lower (or higher) fair value measurement.

## **Table of Contents**

**Cost Method Investments.** For investee companies over which we do not have significant influence and a controlling interest, we carry the investment at cost and recognize as income for any dividend received from distribution of the investee's earnings.

We review our cost method investments for impairment whenever an event or circumstance indicates that an other-than-temporary impairment has occurred. We consider available quantitative and qualitative evidence in evaluating potential impairment of our cost method investments. An impairment charge is recorded if the cost of an investment exceeds its fair value and such excess is determined to be other-than-temporary. Factors we consider in making such a determination include general market conditions, the duration and the extent to which the fair value of an investment is less than its cost, and our intent and ability to hold such investment. As a result of the assessment process for our cost method investments, we recognized a full impairment charge of US\$5.0 million in 2010 for our cost method investment in OpenV, because we had doubts on OpenV's ability to continue as a going concern.

**Allowance for Doubtful Accounts.** We perform ongoing credit evaluations of our customers and generally do not require collateral on accounts receivable. We maintain an allowance for doubtful accounts primarily based upon the aging analysis of the receivables and factors surrounding the credit risk of specific customers.

**Share-based Compensation.** Share-based payment transactions with employees, such as share options, are measured based on the fair value of the equity instrument issued on the date of grant, and are recognized as compensation expense over the requisite service period based on the graded vesting attribution method, with a corresponding impact reflected in additional paid-in capital. We estimated the fair value of our share options at the respective grant dates using the Black-Scholes option-pricing model or the Binomial model.

Under these models, we made a number of assumptions regarding the fair value of the options, including:

the expected future volatility of our ordinary share price;

the risk-free interest rate;

the expected life of options;

the estimated time of vesting of options;

the expected dividend yield;

the exercise price; and

the estimated fair value of our ordinary shares at the grant date for options granted prior to our initial public offering.

For options granted after our initial public offering, the fair value of our ordinary shares on the grant date is determined by the closing trade price of our ADSs representing our ordinary shares on the grant date. For options granted prior to May 16, 2011, we estimated the volatility of the underlying ordinary shares based on the historical stock price volatility of our company and the publicly traded shares of three comparable companies in the digital television and related businesses over a period comparable to the expected term of the options. For options granted after May 16, 2011, we estimated the volatility of the underlying ordinary shares during the life of the options based on the historical stock price volatility of our company over the past years.

A change in any of the terms or conditions of share options will be accounted for as a modification of the plan. Consequently, we calculate incremental compensation cost of a modification as the excess of the fair value of the modified option over the fair value of the original option immediately before its terms are modified, measured based on the share price and other pertinent factors at the modification date. For vested options, we would recognize incremental compensation cost in the period of the modification occurred. For unvested options, we would

recognize, over the remaining requisite service period, the sum of the incremental compensation cost and the remaining unrecognized compensation cost for the original award on the modification date.

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**Table of Contents**

**Consolidation of Variable Interest Entity.** Currently, foreign-invested enterprises incorporated in the PRC are not expressly prohibited from engaging in encryption-related businesses. However, they may have difficulty in obtaining the necessary licenses for the development, production and sale of commercial encryption products in the PRC from the PRC encryption authority due to such authority's generally restrictive approach towards foreign participation in the PRC encryption industry. In addition, SARFT's policy requires any cable television network operator who uses non-PRC CA systems to install a parallel PRC CA system. This policy does not, however, expressly indicate whether the CA systems produced by a foreign-invested company incorporated in the PRC fall into the category of non-PRC CA systems. In light of the above, we conduct substantially all of our business through our operating subsidiary, Super TV, and our variable interest entity, N-S Digital TV, which is wholly owned by PRC citizens and has obtained the licenses for the production and sale of commercial encryption products in the PRC required for our business.

Since the establishment of N-S Digital TV, we have designed the structure such that Super TV is the primary beneficiary of N-S Digital TV:

- (a) The nominee shareholders of N-S Digital TV lack direct or indirect ability to make decisions regarding the activities of N-S Digital TV that could have a significant impact on the economic performance of N-S Digital TV. All of the voting rights of N-S Digital TV's nominee shareholders have been transferred to Super TV such that Super TV has effective control over N-S Digital TV; and
- (b) The nominee shareholders of N-S Digital TV do not have the right to receive the expected residual returns of N-S Digital TV, while such right has been transferred to Super TV such that Super TV is the primary beneficiary of N-S Digital TV.

In order to achieve such purpose, we have entered into a series of contractual agreements with N-S Digital TV and/or its nominee shareholders, including technical support and related services agreement, technology license agreement, technology development agreement, products and software purchase agreement, Equity Transfer Option Agreement, Business Operating Agreement, loan agreements, share pledge agreements and powers of attorney. Through those contractual arrangements, Super TV has the right to: (i) exercise 100% of the voting rights of N-S Digital TV's shareholders and (ii) nominate the members of N-S Digital TV's board of directors and senior management. As a result, Super TV has the power to direct the activities of N-S Digital TV that most significantly impact N-S Digital TV's economic performance, including the power, pursuant to the articles of association of N-S Digital TV, to: (i) approve the operating strategy and investment plan of N-S Digital TV; (ii) elect the members of N-S Digital TV's board of directors and approve their compensation; and (iii) review and approve N-S Digital TV's annual budget and earnings distribution plan. In addition, Super TV has an exclusive and irrevocable option to purchase all of N-S Digital TV's shareholders equity interests in N-S Digital TV at any time. We believe we have substantive kick-out rights pursuant to the terms of the Equity Transfer Option Agreement, and that the terms of the Equity Transfer Option Agreement are currently exercisable and legally enforceable under existing PRC laws, rules and regulations. As a result, we believe the rights of the shareholders of N-S Digital TV effectively accrue to us. Furthermore, the fees we receive from N-S Digital TV under these contractual arrangements are determined by Super TV and may be adjusted by Super TV. For a description of these contractual arrangements, see Item 7. Major Shareholders and Related Party Transactions B. Related Party Transactions.

## **Table of Contents**

As advised by our PRC legal counsel, Han Kun, the ownership structures of our operating subsidiary in China and our consolidated variable interest entity comply with existing PRC laws, rules and regulations. Moreover, Han Kun is of the opinion that each of the agreements that establish the contractual arrangements is valid, legally binding and enforceable and does not violate applicable PRC laws, rules and regulations. However, there exist substantial uncertainties regarding the interpretation and application of PRC laws, rules and regulations, and we cannot assure you that the relevant PRC regulatory authorities will not ultimately determine that these contractual arrangements do not comply with applicable PRC laws, rules and regulations. See Item 3. Key Information D. Risk Factors Risks Related to Our Corporate Structure Our business and operations could be significantly disrupted, and we could be subject to sanctions, if the contractual arrangements between us and our consolidated variable interest entity, N-S Digital TV, which we depend on for the production and sales of our CA systems, are found to be in violation of applicable PRC laws, rules and regulations and Item 3. Key Information D. Risk Factors Risks Related to Our Corporate Structure The shareholders or directors of N-S Digital TV may have conflicts of interest with us.

We have evaluated the VIE structure and concluded that through these contractual arrangements, we have the ability to effectively control N-S Digital TV and its subsidiaries as well as to receive substantially all the economic benefits of those entities. As a result, we are considered the primary beneficiary of N-S Digital TV, and N-S Digital TV and its subsidiaries are our variable interest entities under U.S. GAAP and we consolidate their financial results and assets and liabilities in our consolidated financial statements.

### ***Government Subsidies.***

Government subsidies mainly represent amounts granted by local government authorities as an incentive for companies to promote the development of the local technology industry. We record any government subsidies received with respect to government sponsored projects as liabilities and record such government subsidies as subsidy income when no performance of the relevant obligation is required. Subsidy income of US\$89,000, US\$168,000 and US\$351,000 was recognized in 2010, 2011 and 2012, respectively.

### **Recently Issued Accounting Pronouncements**

See Note 2(aa) to our consolidated financial statements included elsewhere in this annual report for recently issued accounting standards that we believe may have implications on our consolidated financial statements for future periods.

### **Taxes and Incentives**

#### ***Cayman Islands, British Virgin Islands and Hong Kong***

Our company, as an exempted company incorporated in the Cayman Islands, and CDTV BVI, our wholly-owned subsidiary incorporated in BVI, are not subject to any income or capital gains tax under the current laws of the Cayman Islands and BVI. Golden Benefit and CSM Holdings, our indirectly wholly-owned subsidiaries incorporated in Hong Kong, were subject to 16.5% Hong Kong profits tax in 2010, 2011 and 2012 on their activities conducted in Hong Kong.

#### ***PRC***

Our subsidiaries, our variable interest entity and the subsidiaries of our variable interest entity operating in the PRC are subject to PRC taxes as described below:

***Enterprise Income Tax.*** Prior to January 1, 2008, the effective date of the 2008 EIT Law, both domestic and foreign-invested enterprises were generally subject to an enterprise income tax rate of 33% in the PRC under the relevant tax laws then effective. Effective from January 1, 2008, the 2008 EIT Law imposes a tax rate of 25% on all enterprises, including foreign-invested enterprises, and terminates many of the tax exemptions, reductions and preferential treatments available under previous tax laws and regulations. However, under the 2008 EIT Law, enterprises that were established before March 16, 2007 and already enjoy preferential tax treatments will continue to enjoy them (1) in the case of certain preferential tax rates that are specified by tax legislations, for a transition period of five years from January 1, 2008 or (2) in the case of tax exemption or reduction for a specified term, until the expiration of such term.

**Table of Contents**

Each of N-S Digital TV and Super TV was entitled to income tax exemption during the three years from 2004 through 2006, and a 50% reduction of income tax during the subsequent three years from 2007 through 2009. In addition, under the 2008 EIT Law, high-and-new technology enterprises strongly supported by the State are entitled to a preferential tax rate of 15%. In December 2008, N-S Digital TV and Super TV successfully obtained their respective high-and-new technology enterprise certificates under the 2008 EIT Law and were therefore recognized as high-and-new technology enterprises strongly supported by the State and qualified for a preferential tax rate of 15% in each of 2008, 2009 and 2010. In October 2011, N-S Digital TV and Super TV successfully renewed their respective high-and-new technology enterprise certificates and qualified for a preferential tax rate of 15% for another three years from 2011 to 2013. In 2010, Super TV was designated as a key software enterprise by the relevant PRC government authorities and, as a result, qualified for a preferential tax rate of 10% for that year. In March 2013, Super TV's re-application for the key software enterprise designation for the year of 2011 and 2012 was approved by the relevant PRC government authorities. As a result, Super TV would qualify for the 10% preferential tax rate for 2011 and 2012 retroactively.

Each of N-S Media Investment, N-S Investment Holdings and Guangdong R&D was subject to an enterprise income tax rate of 25% in each of 2010, 2011 and 2012. Each of Cyber Cloud, Joysee and Super Movie was subject to an enterprise income tax of 25% in each of 2011 and 2012.

In addition, under the 2008 EIT Law, an enterprise established under the laws of a foreign country or region whose de facto management body is located within the PRC territory is considered a resident enterprise and will generally be subject to the enterprise income tax at the rate of 25% on its global income as well as PRC enterprise income tax reporting obligations. According to the Implementation Rules, de facto management body refers to a managing body that exercises, in substance, overall management and control over the production and business, personnel, accounting and assets of an enterprises. The SAT Notice 82 provides for certain specific criteria for determining whether the de facto management body of a Chinese-controlled offshore enterprise is located in the PRC. In addition, the SAT Bulletin 45, which became effective on September 1, 2011, provides guidance on the implementation of SAT Notice 82. SAT Bulletin 45 clarifies certain issues relating to: (i) the determination procedures of PRC resident enterprise status and (ii) tax registration and other related procedures for PRC resident enterprises. SAT Bulletin 45 also provides that if an offshore PRC resident enterprise presents a copy of the Chinese tax resident determination certificate issued by the competent tax authorities to a payer of PRC-sourced dividends, interest, royalties and other income, such payer shall not withhold income tax on these payments to the offshore PRC resident enterprise. We believe that we are not a PRC resident enterprise with reference to the criteria set forth in the SAT Notice 82. However, if we were to be considered as a PRC resident enterprise, we would be subject to the enterprise income tax at the rate of 25% on our global income as well as PRC enterprise income tax reporting obligations. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China We may be subject to PRC income tax on our global income, or dividends we receive from our PRC subsidiary may be subject to PRC withholding tax, depending on whether we are recognized as a resident enterprise in the PRC. In addition, the 2008 EIT Law and the Implementation Rules provide that a withholding tax of 10% (which may be reduced by the relevant tax treaties between the PRC and other jurisdictions) will generally be applicable to dividends payable to non-resident enterprises, and, unlike the prior tax law, does not specifically exempt corporations that pay dividends from withholding all or part of such income tax when they pay dividends to their non-resident investors. To the extent we are not considered as a PRC resident enterprise or dividends paid from our PRC operating subsidiary are not deemed as dividends among qualified PRC resident enterprises, the dividends our PRC subsidiary pays to us will be subject to this withholding tax. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China We may be subject to PRC income tax on our global income, or dividends we receive from our PRC subsidiary may be subject to PRC withholding tax, depending on whether we are recognized as a resident enterprise in the PRC. In addition, this withholding tax may also apply to dividends we pay to our non-PRC individual shareholders if we were to be considered as a PRC resident enterprise. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China Dividends payable by us to our non-PRC shareholders and ADS holders, and gains on the sales of our ordinary shares or ADSs, may be subject to withholding taxes under PRC tax laws, which may materially reduce the value of your investment.

## **Table of Contents**

**Value-Added Tax and Business Tax.** We are subject to value-added tax, or VAT, at the rate of 17% on the sales of our products. Pursuant to a PRC tax policy intended to encourage the development of software and integrated circuit industries and a notice jointly issued by the PRC Ministry of Finance and the SAT in October 2011, each of N-S Digital TV and Super TV is entitled to a refund of VAT paid at a rate of 14% (i.e., the excess of the effective VAT rate over 3%) of the sale value of some of our software products. The amount of VAT refund included in our total revenues was US\$7.6 million, US\$8.4 million and US\$7.4 million in 2010, 2011 and 2012, respectively, accounting for 8.7%, 8.3% and 8.2%, respectively, of our total revenues in the corresponding periods. We include such refunds in the total revenues in our consolidated statements comprehensive income included elsewhere in this annual report. The VAT refund benefits have been renewed for N-S Digital TV and Super TV from January 1, 2011.

On November 16, 2011, the Ministry of Finance and the SAT issued a pilot tax program under which business tax will be replaced with VAT for certain pilot industries, including, among others, transportation services, research and development and technical services, information technology services and cultural and creative services. The pilot VAT program initially applied only to the pilot industries in Shanghai and has been subsequently expanded to eight additional regions, including, among others, Beijing and Guangdong province. N-S Digital TV, Super TV and each of Super TV's and N-S Digital TV's subsidiaries, all of which are located in Beijing or Guangdong province, fall within the scope of the pilot VAT program and have been recognized as VAT taxpayers since September 1, 2012 or November 1, 2012, the effective time of the pilot VAT program in Beijing and Guangdong province, respectively. Prior to the implementation of such pilot VAT program, each of Super TV's subsidiaries, N-S Digital TV and N-S Digital TV's subsidiaries was subject to business tax at a rate of 5% on certain service-type revenues, including those from our head-end integration services, head-end system development services, licensing income and royalty income. Super TV was exempted from business tax at a rate of 5% on the revenues generated from the technical support, technical training and personnel services it then provided. From September 1, 2012 or November 1, 2012 onwards, as the case may be, each of Super TV's subsidiaries, N-S Digital TV and N-S Digital TV's subsidiaries are required to pay VAT at a rate of 6% for research and development services, technical services and other services deemed by the relevant PRC tax authorities to be within the pilot industries, and is no longer subject to business tax. Super TV is exempted from VAT at a rate of 6% on the revenues generated from the technical support, technical training and personnel services it currently provides.

### ***Tax Arrangement between the PRC and Hong Kong***

The Hong Kong government and the PRC government entered into the *Arrangement for Avoidance of Double Taxation on Income and Prevention of Tax Evasion* on August 21, 2006, which took effect on January 1, 2007 and April 1, 2007 in the PRC and Hong Kong, respectively. This arrangement provides certain tax incentives to use a Hong Kong company as an intermediate holding company for holding investments in the PRC. The withholding tax rate applicable to dividends received by a Hong Kong resident enterprise from its investments in the PRC is 5% compared to the 10% withholding tax rate applicable to dividends received by a company incorporated in a jurisdiction where there is no similar tax treaty or arrangement with the PRC, provided, among others, that the Hong Kong resident enterprise owns at least 25% of the shareholding of the PRC company at all times within the 12-month period immediately preceding the distribution of dividends. In addition, a full tax exemption in the PRC is available on a capital gain derived by a Hong Kong resident enterprise from the disposal of its shares in a PRC company, provided that the Hong Kong resident enterprise owns less than 25% of the shareholding of the PRC company at all times within the 12-month period immediately preceding the distribution of dividends and the assets of the PRC company do not consist mainly of real property situated in the PRC.

The SAT issued the SAT Notice 601 and the SAT Announcement 30 on October 27, 2009 and June 29, 2012, respectively, both of which are applicable to the tax arrangements between PRC and Hong Kong. Specifically, the SAT Notice 601 provides that only the enterprises with active operations can be recognized as "beneficial owners" under relevant tax treaties which are entitled to enjoy the corresponding tax benefits. It further provides that those enterprises that are established solely for the purposes of benefiting from favorable tax treatment under the relevant tax treaties should not be recognized as "beneficial owners" and therefore cannot enjoy favorable tax treatment. Furthermore, SAT Announcement 30 provides that a comprehensive analysis should be made when determining the "beneficial owner" status based on all the factors set out in the SAT Notice 601. See Item 3. Key Information D. Risk Factors We may be subject to PRC income tax on our global income, or dividends we receive from our PRC subsidiary may be subject to PRC withholding tax, depending on whether we are recognized as a resident enterprise in the PRC.

**Table of Contents****Recent Acquisitions**

See Item 4. Information on the Company A. History and Development of the Company Our Investments and Acquisitions.

**Results of Operations**

The following table sets forth our condensed consolidated statements of operations by amount and as a percentage of our net revenues for the periods indicated:

|   | 2010        |                         | For the years ended December 31,<br>2011 |                         | 2012        |                         |
|---|-------------|-------------------------|--|-------------------------|-------------|-------------------------|
|   | Amount      | % of<br>Net<br>Revenues | Amount                                   | % of<br>Net<br>Revenues | Amount      | % of<br>Net<br>Revenues |
| (In thousands, except percentages)                                |             |                         |  |                         |             |                         |
| <b>Revenues:</b>  |             |                         |  |                         |             |                         |
| Products  | US\$ 82,518 | 94.7%                   | US\$ 95,162                              | 96.1%                   | US\$ 85,319 | 96.1%                   |
| Services  | 5,225       | 6.0                     | 5,378                                    | 5.4                     | 4,925       | 5.5                     |
| Total revenues  | 87,743      | 100.7                   | 100,540                                  | 101.5                   | 90,244      | 101.7                   |
| Business taxes  | (620)       | (0.7)                   | (1,445)                                  | (1.5)                   | (1,501)     | (1.7)                   |
| Net revenues  | 87,123      | 100.0                   | 99,095                                   | 100.0                   | 88,743      | 100.0                   |
| <b>Cost of revenues:<sup>(1)</sup></b>                            |             |                         |  |                         |             |                         |
| Products  | 15,148      | 17.4                    | 16,100                                   | 16.2                    | 16,880      | 19.0                    |
| Services  | 3,040       | 3.5                     | 3,027                                    | 3.1                     | 3,952       | 4.5                     |
| Total cost of revenues  | 18,188      | 20.9                    | 19,127                                   | 19.3                    | 20,832      | 23.5                    |
| Gross profit  | 68,935      | 79.1                    | 79,968                                   | 80.7                    | 67,911      | 76.5                    |
| <b>Operating expenses:</b>  |             |                         |  |                         |             |                         |
| Research and development expenses <sup>(1)</sup>                  | 10,432      | 12.0                    | 13,140                                   | 13.3                    | 17,402      | 19.6                    |
| Selling and marketing expenses <sup>(1)</sup>                     | 8,504       | 9.8                     | 12,377                                   | 12.5                    | 13,606      | 15.3                    |
| General and administrative expenses <sup>(1)</sup>                | 6,389       | 7.3                     | 9,723                                    | 9.8                     | 9,444       | 10.6                    |
| Total operating expenses  | 25,325      | 29.1                    | 35,240                                   | 35.6                    | 40,452      | 45.6                    |
| Income from operations  | 43,610      | 50.1                    | 44,728                                   | 45.1                    | 27,459      | 30.9                    |
| <b>Non-operating income/(expenses)</b>                            |             |                         |  |                         |             |                         |
| Interest income   | 5,294       | 6.0                     | 6,810                                    | 6.9                     | 6,318       | 7.1                     |
| Interest expense  |             |                         | (1,452)                                  | (1.5)                   | (739)       | (0.8)                   |
| Gain/(loss) from forward contracts                                |             |                         | 404                                      | 0.4                     | (690)       | (0.8)                   |
| Impairment loss on long-term investments                          | (5,000)     | (5.7)                   |  |                         | (4,487)     | (5.1)                   |
| Other (expense)/income  | (92)        | (0.1)                   | 594                                      | 0.6                     | 549         | 0.6                     |
| Income before income taxes  | 43,812      | 50.3                    | 51,084                                   | 51.5                    | 28,410      | 32.0                    |
| Income tax expense  | 10,250      | 11.7                    | 9,762                                    | 9.8                     | 22,232      | 25.1                    |
| Net income before income/(loss) from equity<br>method investments | 33,562      | 38.6                    | 41,322                                   | 41.7                    | 6,178       | 7.0                     |

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|  |             |       |             |       |            |       |
|--|-------------|-------|-------------|-------|------------|-------|
| Loss from equity method investments, net of income taxes | (151)       | (0.2) | (1,052)     | (1.1) | (640)      | (0.7) |
| Net income   | 33,411      | 38.4  | 40,270      | 40.6  | 5,538      | 6.2   |
| Net loss attributable to noncontrolling interest         | 10          | 0.0   | 730         | 0.8   | 1,389      | 1.6   |
| Net income attributable to holders of ordinary shares    | US\$ 33,421 | 38.4% | US\$ 41,000 | 41.4% | US\$ 6,927 | 7.8%  |

(1) Share-based compensation charges incurred during the period related to:

**Table of Contents**

|                                     | 2010                               |                   | For the years ended December 31,<br>2011 |                   | 2012       |                   |
|-------------------------------------|------------------------------------|-------------------|--|-------------------|------------|-------------------|
|                                     | Amount                             | % of Net Revenues | Amount                                   | % of Net Revenues | Amount     | % of Net Revenues |
|                                     | (In thousands, except percentages) |                   |  |                   |            |                   |
| Cost of revenues                    | US\$ 10                            | 0.0%              | US\$ 52                                  | 0.1%              | US\$ 5     | 0.0%              |
| Research and development expenses   | 393                                | 0.5               | 1,025                                    | 1.0               | 552        | 0.6               |
| Selling and marketing expenses      | 384                                | 0.4               | 633                                      | 0.6               | 356        | 0.4               |
| General and administrative expenses | US\$ 691                           | 0.8%              | US\$ 3,852                               | 3.9%              | US\$ 1,701 | 1.9%              |

**Comparison of Years Ended December 31, 2012 and December 31, 2011**

**Revenues.** The following table sets forth revenues by sources and the percentage of our total revenues for the periods indicated:

|                             | 2011                               |                     | For the years ended December 31,<br>2012 |                     |
|-----------------------------|------------------------------------|---------------------|--|---------------------|
|                             | Amount                             | % of Total Revenues | Amount                                   | % of Total Revenues |
|                             | (In thousands, except percentages) |                     |  |                     |
| <b>Products</b>             |                                    |                     |  |                     |
| Smart cards                 | US\$ 91,960                        | 91.5%               | US\$ 75,185                              | 83.3%               |
| Other products              | 3,202                              | 3.2                 | 10,134                                   | 11.2                |
| Subtotal                    | 95,162                             | 94.7                | 85,319                                   | 94.5                |
| <b>Services</b>             |                                    |                     |  |                     |
| Head-end system integration | 2,562                              | 2.6                 | 2,175                                    | 2.5                 |
| Head-end system development | 736                                | 0.7                 | 987                                      | 1.1                 |
| Licensing income            | 1,328                              | 1.3                 | 1,246                                    | 1.4                 |
| Royalty income              | 742                                | 0.7                 | 382                                      | 0.4                 |
| Other services              | 10                                 | 0.0                 | 135                                      | 0.1                 |
| Subtotal                    | 5,378                              | 5.3                 | 4,925                                    | 5.5                 |
| <b>Total revenues</b>       | US\$ 100,540                       | 100.0%              | US\$ 90,244                              | 100.0%              |

Our total revenues decreased by 10.2% from US\$100.5 million in 2011 to US\$90.2 million in 2012, reflecting a decrease in the revenue from the sales of our products.

Revenues from the sales of our products decreased by 10.3% from US\$95.2 million in 2011 to US\$85.3 million in 2012, principally as a result of a decrease in the shipment volume of smart cards coupled with a decline of 2.5% in the average selling price, or the ASP, of smart cards, which was partially offset by an increase in the sales of other products, such as surface mounted device chips and multimedia home entertainment boxes. The decrease in the shipment volume of smart cards in 2012 reflected a reduction in market demand as a result of the provincial-level cable network consolidation and the cable television digitalization process in China. The increase in the sales of other products was primarily attributable to an increase in the sales of surface mounted device chips.

**Table of Contents**

Revenues from the sales of our services decreased by 8.4% from US\$5.4 million in 2011 to US\$4.9 million in 2012, largely due to decreases in revenues from royalty income and head-end system integration, which were principally attributable to deeper discounts we offered to our customers in light of the intense market competition.

**Net Revenues.** Our net revenues decreased by 10.4% from US\$99.1 million in 2011 to US\$88.7 million in 2012.

**Cost of Revenues.** The following table sets forth cost of revenues by sources of revenues by amount and as a percentage of net revenues for the periods indicated:

|                               | 2011               |   | Years ended December 31, 2012 |                   |
|-------------------------------|--------------------|---|-------------------------------|-------------------|
|                               | Amount             | % of Net Revenues<br>(In thousands, except percentages) | Amount                        | % of Net Revenues |
| Products                      | US\$ 16,100        | 16.2%   | US\$ 16,880                   | 19.0%             |
| Services                      | 3,027              | 3.1   | 3,952                         | 4.5               |
| <b>Total cost of revenues</b> | <b>US\$ 19,127</b> | <b>19.3%</b>  | <b>US\$ 20,832</b>            | <b>23.5%</b>      |

Cost of revenues increased by 8.9% to US\$20.8 million in 2012 from US\$19.1 million in 2011, primarily reflecting an increase in costs relating to our services, and, to a lesser extent, an increase in costs relating to our products. Cost of revenues relating to our products increased by 4.8% to US\$16.9 million in 2012 from US\$16.1 million in 2011, principally due to an increase in the cost of sales of other products, which was partially offset by a decrease in the cost of sales of smart cards. Cost of revenues relating to our services increased by 30.6% to US\$4.0 million in 2012 from US\$3.0 million in 2011, mainly due to an increase in the cost of head-end system integration.

**Gross Profit and Gross Margin.** Gross profit decreased by 15.1% from US\$80.0 million in 2011 to US\$67.9 million in 2012. Our gross margin decreased from 80.7% in 2011 to 76.5% in 2012, principally as a result of a decrease in the ASP of smart cards, coupled with a decrease in smart card sales and an increase in the sales of other products, which have lower gross margins than smart cards.

**Operating Expenses.** Our operating expenses increased by 14.8% to US\$40.5 million in 2012 from US\$35.2 million in 2011. This increase largely reflected increases in research and development expenses and sales and marketing expenses. Operating expenses, as a percentage of net revenues, increased to 45.6% in 2012 from 35.6% in 2011. We expect operating expenses will increase as we continue to increase our spending on the research and development and commercialization of our new solutions and products.

**Research and Development Expenses.** Our research and development expenses increased by 32.4% to US\$17.4 million in 2012 from US\$13.1 million in 2011. This increase was primarily due to an increase in office rental and personnel related expenses resulting from an increase in the number of our research and development staff, which was partially offset by a decrease in share-based compensation expenses. Our research and development expenses, as a percentage of net revenues, increased to 19.6% in 2012 from 13.3% in 2011.

**Selling and Marketing Expenses.** Our selling and marketing expenses increased by 9.9% to US\$13.6 million in 2012 from US\$12.4 million in 2011. This increase was mainly attributable to an increase in personnel related expenses resulting from an increase in the number of our sales and marketing staff. Our selling and marketing expenses, as a percentage of net revenues, increased to 15.3% in 2012 from 12.5% in 2011.

**General and Administrative Expenses.** Our general and administrative expenses decreased by 2.9% to US\$9.4 million in 2012 from US\$9.7 million in 2011, primarily reflecting a decrease in share-based compensation expenses.

**Table of Contents**

**Income from Operations.** As a result of the foregoing, our income from operations decreased by 38.6% from US\$44.7 million in 2011 to US\$27.5 million in 2012.

**Non-Operating Income (Expenses).** We had non-operating income of US\$1.0 million in 2012 compared to US\$6.4 million in 2011. Our non-operating income in 2012 primarily consisted of interest income of US\$6.3 million and other income of US\$0.6 million, which was partially offset by an impairment loss on long-term investments of US\$4.5 million, interest expenses of US\$0.7 million and loss from foreign currency forward contracts of US\$0.7 million. Our interest income decreased by 7.2% from US\$6.8 million in 2011 to US\$6.3 million in 2012, primarily due to a decrease in the average balance of our bank deposits. In 2012, we fully accrued an impairment charge of US\$4.5 million related to our investment in 3DiJoy based on the fair value of 3DiJoy we estimated with the assistance of a third party valuation firm, as we had doubts regarding 3DiJoy's ability to operate as a going concern given that it had been experiencing financial difficulties and had failed to obtain new capital funding from its shareholders or otherwise. To facilitate the payment of the special cash dividend declared in November 2010, we entered into foreign currency forward contracts in April and May 2011, which met the definition of derivatives and were measured at fair value. The change in the forward rate for U.S. dollar against the Renminbi from the last date of each year to the expiration dates of the foreign currency forward contracts was recognized as gain or loss from foreign currency forward contracts. We also incurred interest expenses of US\$1.5 million and US\$0.7 million in 2011 and 2012, respectively, as we borrowed short-term loans in connection with the above-mentioned foreign currency forward contracts.

**Income Tax Expenses.** Our income tax expenses increased from US\$9.8 million in 2011 to US\$22.2 million in 2012. The increase in our income tax expenses was primarily due to (i) a US\$9.3 million withholding tax in connection with the repatriation of dividends outside of the PRC in 2012 and (ii) the accrual of a US\$4.8 million deferred tax liability related to the undistributed retained earnings of our PRC subsidiary as a result of our decision in 2012 to distribute the undistributed retained earnings of our PRC subsidiary, which was partially offset by a decrease in taxable income.

**Income/(Loss) from Equity Method Investments, Net of Income Taxes.** Our loss from equity method investments decreased from US\$1.1 million in 2011 to US\$0.6 million in 2012. The decrease was mainly due to a gain from our equity method investment in Guangzhou Rujia, which was partially offset by the loss from our equity method investments in Xinghe Union and Shibo Movie.

**Net Loss Attributable to Noncontrolling Interest.** Net loss attributable to noncontrolling interest increased from US\$0.7 million in 2011 to US\$1.4 million in 2012. Net loss attributable to noncontrolling interest represents the proportional share of net loss of our consolidated, but not wholly-owned, subsidiaries that are attributable to the other shareholders of such subsidiaries. The change was primarily due to the loss of our majority-owned subsidiaries, in particular, Joysee and Cyber Cloud.

**Net Income Attributable to Holders of Ordinary Shares.** As a result of the foregoing, net income attributable to holders of ordinary shares decreased by 83.1% from US\$41.0 million in 2011 to US\$6.9 million in 2012. Our basic and diluted earnings per ordinary share in 2012 were US\$0.12 and US\$0.12, respectively.

**Comparison of Years Ended December 31, 2011 and December 31, 2010**

**Revenues.** The following table sets forth revenues by sources and the percentage of our total revenues for the periods indicated:

**Table of Contents**

|                             | For the years ended December 31, |   |                     |                     |
|-----------------------------|----------------------------------|---|---------------------|---------------------|
|                             | 2010                             |   | 2011                |                     |
|                             | Amount                           | % of Total Revenues<br>(In thousands, except percentages) | Amount              | % of Total Revenues |
| <b>Products</b>             |                                  |   |                     |                     |
| Smart cards                 | US\$ 82,153                      | 93.6%   | US\$ 91,960         | 91.5%               |
| Other products              | 365                              | 0.4   | 3,202               | 3.2                 |
| Subtotal                    | 82,518                           | 94.0  | 95,162              | 94.7                |
| <b>Services</b>             |                                  |   |                     |                     |
| Head-end system integration | 2,399                            | 2.7   | 2,562               | 2.6                 |
| Head-end system development | 595                              | 0.7   | 736                 | 0.7                 |
| Licensing income            | 1,565                            | 1.8   | 1,328               | 1.3                 |
| Royalty income              | 662                              | 0.8   | 742                 | 0.7                 |
| Other services              | 4                                | 0.0   | 10                  | 0.0                 |
| Subtotal                    | 5,225                            | 6.0   | 5,378               | 5.3                 |
| <b>Total revenues</b>       | <b>US\$ 87,743</b>               | <b>100.0%</b>   | <b>US\$ 100,540</b> | <b>100.0%</b>       |

Our total revenues increased by 14.6% to US\$100.5 million in 2011 from US\$87.7 million in 2010, reflecting an increase in the revenue from the sales of our products.

Revenues from the sales of our products increased by 15.3% to US\$95.2 million in 2011 from US\$82.5 million in 2010, principally as a result of a significant increase in the shipment volume of smart cards and other related products, such as integrated chips and surface mounted device chips, which was partially offset by a decline of 1.0% in the ASP of smart cards.

Revenues from the sales of our services increased by 2.9% to US\$5.4 million in 2011 from US\$5.2 million in 2010.

**Net Revenues.** Our net revenues increased by 13.7% to US\$99.1 million in 2011 from US\$87.1 million in 2010.

**Cost of Revenues.** The following table sets forth cost of revenues by sources of revenues by amount and as a percentage of net revenues for the periods indicated:

|                               | Years ended December 31, |   |                    |                   |
|-------------------------------|--------------------------|---|--------------------|-------------------|
|                               | 2010                     |   | 2011               |                   |
|                               | Amount                   | % of Net Revenues<br>(In thousands, except percentages) | Amount             | % of Net Revenues |
| Products                      | US\$ 15,148              | 17.4%   | US\$ 16,100        | 16.2%             |
| Services                      | 3,040                    | 3.5   | 3,027              | 3.1               |
| <b>Total cost of revenues</b> | <b>US\$ 18,188</b>       | <b>20.9%</b>  | <b>US\$ 19,127</b> | <b>19.3%</b>      |

Cost of revenues increased by 5.2% to US\$19.1 million in 2011 from US\$18.2 million in 2010, primarily reflecting an increase in costs relating to our products, which was partially offset by a decrease in costs relating to our services. Cost of revenues relating to our products increased by 6.3% to US\$16.1 million in 2011 from US\$15.1 million in 2010, corresponding to the increases in shipment volumes of smart cards and other related products. Cost of revenues relating to our services slightly decreased by 0.4% to US\$3.03 million in 2011 from US\$3.04 million in 2010.

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**Table of Contents**

**Gross Profit and Gross Margin.** Gross profit increased by 16.0% to US\$80.0 million in 2011 from US\$68.9 million in 2010. Our gross margin increased to 80.7% in 2011 from 79.1% in 2010, principally as a result of a decrease in the unit cost of smart cards by 10.0% compared to 2010.

**Operating Expenses.** Our operating expenses increased by 39.2% to US\$35.2 million in 2011 from US\$25.3 million in 2010. This increase largely reflected increases in research and development expenses, selling and marketing expenses and general and administrative expenses. Operating expenses, as a percentage of net revenues, increased to 35.6% in 2011 from 29.1% in 2010. We expect operating expenses will increase as we continue to increase our spending on the research and development and commercialization of our new solutions and products.

**Research and Development Expenses.** Our research and development expenses increased by 26.0% to US\$13.1 million in 2011 from US\$10.4 million in 2010. This increase was primarily due to increases in the average salary of research and development staff and share-based compensation expenses relating to options granted to research and development staff in 2011. Our research and development expenses, as a percentage of net revenues, increased to 13.3% in 2011 from 12.0% in 2010.

**Selling and Marketing Expenses.** Our selling and marketing expenses increased by 45.5% to US\$12.4 million in 2011 from US\$8.5 million in 2010. This increase was mainly attributable to increases in marketing activities and the average salary of sales and marketing staff. Our selling and marketing expenses, as a percentage of net revenues, increased to 12.5% in 2011 from 9.8% in 2010.

**General and Administrative Expenses.** Our general and administrative expenses increased by 52.2% to US\$9.7 million in 2011 from US\$6.4 million in 2010. This increase was principally a result of an increase in share-based compensation expenses relating to options granted to general and administrative staff in 2011.

**Income from Operations.** As a result of the foregoing, our income from operations increased by 2.6% from US\$43.6 million in 2010 to US\$44.7 million in 2011.

**Non-Operating Income (Expenses).** We had non-operating income of US\$6.4 million in 2011 compared to US\$0.2 million in 2010. Our non-operating income in 2011 primarily consisted of interest income of US\$6.8 million, gain from foreign currency forward contracts of US\$0.4 million and other income of US\$0.6 million, which was partially offset by interest expenses of US\$1.5 million. Our interest income increased by 28.6% to US\$6.8 million in 2011 from US\$5.3 million in 2010, principally as a result of the increase in both the average balance of our bank deposits and the average interest rates. To facilitate the payment of the special cash dividend declared in November 2010, we entered into foreign currency forward contracts in April and May 2011, which met the definition of derivatives and were measured at fair value. The change in the forward rate for U.S. dollar against the Renminbi from the last date of each year to the expiration dates of the foreign currency forward contracts was recognized as gain from foreign currency forward contracts. In 2011, we also incurred interest expenses of US\$1.5 million as we borrowed short-term loans in connection with the above-mentioned foreign currency forward contracts. In 2010, we incurred a US\$5.0 million impairment charge as we wrote off our entire investment in OpenV.

**Income Tax Expenses.** Our income tax expenses decreased by 4.8% from US\$10.3 million in 2010 to US\$9.8 million in 2011. While our income tax expenses in 2010 reflected a US\$5.4 million withholding tax in connection with the repatriation of dividends outside of the PRC, we generated higher taxable income and had less tax exemptions in 2011.

**Income/(Loss) from Equity Method Investments, Net of Income Taxes.** Our loss from equity method investments increased from US\$0.2 million in 2010 to US\$1.1 million in 2011. The change was mainly as a result of the increased loss from our equity method investments in 3DiJoy and Guangzhou Rujia.

**Net Loss Attributable to Noncontrolling Interest.** Net loss attributable to noncontrolling interest increased from US\$10,000 in 2010 to US\$0.7 million in 2011. Net loss attributable to noncontrolling interest represents the proportional share of net loss of our consolidated, but not wholly-owned, subsidiaries that are attributable to the other shareholders of such subsidiaries. The change was primarily due to the loss of majority-owned subsidiaries we established in 2011.

**Table of Contents**

**Net Income Attributable to Holders of Ordinary Shares.** As a result of the foregoing, net income attributable to holders of ordinary shares increased by 22.7% to US\$41.0 million in 2011 from US\$33.4 million in 2010. Our basic and diluted earnings per ordinary share in 2011 were US\$0.70 and US\$0.69, respectively.

**B. Liquidity and Capital Resources****Liquidity**

|   | For the years ended December 31, |                |                |
|---|----------------------------------|----------------|----------------|
|   | 2010                             | 2011           | 2012           |
|   |                                  | (In thousands) |                |
| Cash and cash equivalents                 | US\$ 148,944                     | US\$ 201,557   | US\$ 130,697   |
| Net cash provided by operating activities | 32,573                           | 37,685         | 20,897         |
| Net cash provided by investing activities | 19,626                           | 18,011         | 55,025         |
| Net cash used in financing activities     | US\$ (39,033)                    | US\$ (15,048)  | US\$ (147,214) |

**Operating Activities.** Net cash provided by operating activities was US\$20.9 million in 2012, which was primarily derived from our net income of US\$5.5 million, adjusted to reflect the adding back of US\$4.5 million in impairment loss on long-term investments, US\$2.6 million share-based compensation charges, a US\$4.2 million increase in deferred income taxes, a US\$2.8 million increase in accrued expenses and other current liabilities and a US\$2.0 million increase in government subsidies. Cash provided by operating activities in 2012 was partially offset by a US\$3.1 million increase in accounts receivable and a US\$2.0 million increase in inventories.

Net cash provided by operating activities was US\$37.7 million in 2011, which was primarily derived from our net income of US\$40.3 million, adjusted to reflect the adding back of US\$5.6 million share-based compensation charges, US\$1.3 million in depreciation and amortization costs and US\$1.1 million loss from equity method investment, a US\$1.8 million increase in government subsidies, a US\$1.8 million increase in income tax payable and a US\$1.5 million increase in deferred revenues. Net income was partially offset by a US\$13.7 million increase in accounts receivable. The significant increase in accounts receivable largely reflected more favorable credit terms awarded to our major customers due to intense competition and tighter bank lending policies to which our major customers are subject.

Net cash provided by operating activities was US\$32.6 million in 2010, which was primarily derived from our net income of US\$33.4 million, adjusted to reflect the adding back of US\$5.0 million in impairment loss of cost method investment, US\$1.3 million in depreciation and amortization costs and US\$1.5 million share-based compensation charges. Net income was partially offset by a US\$11.7 million increase in accounts receivable, a US\$2.4 million increase in prepaid expenses and other current assets, and a US\$1.4 million decrease in income tax payable. The significant increase in accounts receivable largely reflected a significant increase in revenues in the later part of 2010.

**Investing Activities.** Net cash provided by investing activities was US\$55.0 million in 2012, primarily consisting of the release of US\$55.5 million bank deposits pledged as security for the short-term loans we borrowed in 2011 in connection with the foreign currency forward contracts, which was partially offset by an aggregate of US\$1.6 million in connection with our investments in Shibo Movie and Xinghe Union in 2012.

Net cash provided by investing activities was US\$18.0 million in 2011, primarily consisting of a withdrawal of US\$41.7 million from our bank deposits maturing over three months, an aggregate of US\$26.6 million in proceeds from the disposal of held-to-maturity corporate and PRC government bonds and a US\$6.8 million from refund of deposit for investment in Cyber Cloud, which was partially offset by (i) US\$55.5 million bank deposits pledged as security for the short-term loans we borrowed in 2011 in connection with the foreign currency forward contracts and (ii) a US\$2.0 million decrease in cash as a result of de-consolidating Dongguan SuperTV following its cessation to be a subsidiary in 2011 due to the disposition of our equity ownership in Dongguan.

Net cash provided by investing activities was US\$19.6 million in 2010, primarily consisting of an aggregate of US\$37.8 million in proceeds from held to maturity corporate and PRC government bonds, a withdrawal of US\$25.0 million from our bank deposits maturing over three months, interest income of US\$1.4 million from held-to-maturity investments, which was partially offset by an aggregate of US\$24.8 million used to purchase additional corporate and government bonds, an aggregate of US\$13.5 million used in long term investment and US\$6.8 million used in prepaid investment.



## **Table of Contents**

**Financing Activities.** Net cash used in financing activities was US\$147.2 million in 2012, primarily reflecting a US\$92.1 million special cash dividend paid to our shareholders and the repayment of short-term loans in an aggregate principal amount of US\$55.2 million that we borrowed in 2011 in connection with the foreign currency forward contracts.

Net cash used in financing activities was US\$15.0 million in 2011, primarily consisting of a US\$77.2 million special cash dividend paid to our shareholders, which was partially offset by short-term loans in an aggregate principal amount of US\$55.2 million we borrowed in connection with the foreign currency forward contracts and a US\$6.5 million capital injection by noncontrolling shareholders of our majority-owned subsidiaries.

Net cash used in financing activities was US\$39.0 million in 2010, consisting of a US\$40.3 million special cash dividend paid to our shareholders, which was partially offset by US\$1.3 million in proceeds from the exercise of our share options by employees.

According to the revised *PRC Company Law*, which took effect on January 1, 2006, our subsidiaries and variable interest entities in the PRC are required to make appropriations to the statutory surplus reserve which are still required to be made at the rate of 10% of profits after tax as determined under PRC GAAP until the balance of such reserve fund reaches 50% of the entities' registered capital.

Our subsidiaries and our variable interest entities in the PRC may, upon a resolution passed by their respective shareholders, convert the statutory surplus reserve into capital. The statutory reserve represents appropriations of retained earnings determined according to PRC law and may not be distributed. There were no appropriations to reserves other than to those of our subsidiaries and our variable interest entity in the PRC during any of the periods presented. However, as a result of these laws, approximately US\$17.7 million and US\$17.9 million of our retained earnings were not available for distribution as of December 31, 2011 and December 31, 2012, respectively.

As a holding company, our ability to pay dividends and other cash distributions to our shareholders depends in part upon dividends and other distributions paid to us by our PRC subsidiary, Super TV. The amount of dividends paid by Super TV to us primarily depends on the service fees paid to Super TV from N-S Digital TV, and, to a lesser degree, Super TV's retained earnings. As of December 31, 2011 and 2012, the total amount of service fees payable to Super TV from N-S Digital TV under the contractual agreements was US\$6.0 million and US\$23.5 million, respectively. Conducting our operations through contractual arrangements with N-S Digital TV entails a risk that we may lose the power to direct the activities that most significantly affect the economic performance of N-S Digital TV, which may result in our being unable to consolidate its financial results with our results and may impair our access to its cash flow from operations and thereby reduce our liquidity. See Item 3. Key Information D. Risk Factors Risks Related to Our Corporate Structure for more information.

In 2010, 2011 and 2012, N-S Digital TV and its subsidiaries in aggregate contributed 91.4%, 93.1% and 89.0%, respectively, of our total net revenues. Our operations not conducted through contractual arrangements with N-S Digital TV primarily consist of the sales of multimedia home entertainment boxes and cloud computing technology-based services, accounting for 8.6%, 6.9% and 11.0% of our total net revenues in 2010, 2011 and 2012, respectively. As of December 31, 2011 and 2012, N-S Digital TV and its subsidiaries accounted for an aggregate of 16.9% and 31.6%, respectively, of our total assets, and 10.6% and 11.8%, respectively, of our total liabilities. The assets not associated with N-S Digital TV primarily consist of cash and cash equivalents, equity method investments, and property and equipment.

## **Capital Expenditures**

In 2010, 2011 and 2012, our capital expenditures totaled US\$20.9 million, US\$0.7 million and US\$2.4 million, respectively. Our capital expenditures in 2012 primarily consisted of US\$1.6 million in long-term investment and US\$0.8 million used to purchase computers and other electronic equipment.

We believe that our current levels of cash and cash equivalents, and cash flows from operations in the near future, will be sufficient to meet our anticipated capital expenditure and other cash needs for at least the next 12 months. However, we may need additional cash resources in the future if we experience changed business conditions or other developments. We also may need additional cash resources in the future if we find and wish to pursue opportunities for investment, acquisition, strategic cooperation or other similar actions. If we ever determine that our cash requirements exceed our amounts of cash and cash equivalents on hand, we may seek to issue debt or equity securities or obtain a credit facility. Any issuance of equity securities could cause dilution for our shareholders. Any incurrence of indebtedness could increase our debt service obligations and cause us to be subject to restrictive operating and finance covenants. It is possible that, when we need additional cash resources, financing will be available to us only in amounts or on terms that would not be acceptable to us or financing will not be available at all.

## **C. Research and Development, Patents and Licenses, etc.**

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See Item 4. Information on the Company B. Business Overview Research and Development for information relating to our research and development.

See Item 4. Information on the Company B. Business Overview Intellectual Property for information relating to our intellectual property.

**Table of Contents****D. Trend Information**

Other than as disclosed elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events for the period from January 1, 2010 to December 31, 2012 that are reasonably likely to have a material adverse effect on our net revenues, income, profitability, liquidity or capital resources, or that would cause the disclosed financial information to be not necessarily indicative of future operating results or financial conditions.

**E. Off-Balance Sheet Arrangements**

We have not entered into any financial guarantees or other commitments to guarantee the payment obligations of any third parties. We have not entered into any derivative contracts that are indexed to our shares and classified as shareholders' equity or that are not reflected in our consolidated financial statements. Furthermore, we do not have any retained or contingent interest in assets transferred to an unconsolidated entity that serves as credit, liquidity or market risk support to such entity. We do not have any 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.

**F. Tabular Disclosure of Contractual Obligations**

The following table sets forth our contractual obligations as of December 31, 2012:

|  | Contractual Obligations |            |                             |                      | Total        |
|--|-------------------------|------------|-----------------------------|----------------------|--------------|
|  | Less than<br>1 Year     | 1-3 Years  | 3-5 Years<br>(In thousands) | More than<br>5 Years |              |
| Operating lease obligations <sup>(1)</sup> | 1,208                   | 315        |                             |                      | 1,523        |
| Purchase obligations                       | 351                     |            |                             |                      | 351          |
| <b>Total</b>                               | <b>1,559</b>            | <b>315</b> |                             |                      | <b>1,874</b> |

(1) Operating leases generally relate to the lease of our office premises.

**Item 6. Directors, Senior Management and Employees****A. Directors and Senior Management**

Our board of directors consists of seven directors, including four independent directors. The following table sets forth certain information concerning our directors and executive officers as of April 15, 2013.

| Name                 | Age | Position                              |
|----------------------|-----|---------------------------------------|
| Jianhua ZHU          | 43  | Chairman and Chief Executive Officer  |
| Zengxiang LU         | 42  | Director                              |
| James Hsiang Ming HO | 53  | Director                              |
| Jianyue PAN          | 45  | Independent Director                  |
| Eric Zhe XU          | 37  | Independent Director                  |
| Chaoyang XIA         | 43  | Independent Director                  |
| Songzuo XIANG        | 48  | Independent Director                  |
| Zhenwen LIANG        | 39  | Chief Financial Officer               |
| Dong LI              | 41  | President and Chief Marketing Officer |
| Tianxing WANG        | 44  | Chief Technology Officer              |
| Huiqing CHEN         | 40  | Chief Administrative Officer          |

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*Jianhua ZHU*, one of our founders, has served as the chairman of our board of directors since November 2008 and as chief executive officer of our company since December 2006 and has been a director since 2004. He was the chairman of our board of directors from 2004 until December 2006. From 2001 until 2004, Mr. Zhu was general manager of N-T Information Engineering. From 1998 until 2001, he was deputy general manager of N-T Information Engineering. He has also been the supervisor of N-T Information Engineering since 2006. Mr. Zhu was the executive director of Guangdong R&D prior to April 2010. He worked at the China Technology Import and Export Corp. from 1994 until 1997. Mr. Zhu holds bachelor's and master's degrees in precision instrumentation from Tsinghua University.

**Table of Contents**

*Zengxiang LU*, one of our founders, has been a board member since 2004. He was chairman of our board of directors and our chief strategy officer from December 2006 until November 2008 and chief executive officer from 2004 until December 2006. Dr. Lu was the president of Guangdong R&D prior to April 2010 and was also a director from 2005 until 2007. Dr. Lu worked on the development of CA systems at Tsinghua Tongfang from 1999 to August 2001. He was deputy general manager of N-T Information Engineering from August 2001 until 2004, and has served on the board of N-T Information Engineering since 1998. Dr. Lu holds a bachelor's degree in automation and a doctorate degree in signal processing from Tsinghua University.

*James Hsiang Ming HO* has been a director of our company since November 2006. Mr. Ho is a vice president of Capital International, Inc., responsible for private equity in Asia. Prior to joining Capital International, Inc. in 1996, Mr. Ho was vice president of global equity investments at the Bank of America in Hong Kong. Mr. Ho was formerly a director of Pacific Textiles Holdings, Ltd., a Hong-Kong listed company, Renhe Commercial Holdings Company Limited, also a Hong Kong-listed company, and On\*Media Corporation, a South Korea-listed company. He received a bachelor's degree in economics from the National Taiwan University and a Master of Business Administration degree from the Wharton School of Business at the University of Pennsylvania.

*Jianyue PAN* has been an independent director of our company since December 2010. Mr. Pan serves as the global vice president and Asia Pacific president of Synopsys, Inc, a worldwide leading company in electronic design automation software and IP for semiconductor design. Since 1995, Mr. Pan has held different positions at Synopsys, including China chief representative and director of China sales. Prior to Synopsys, Mr. Pan held sales and management roles in Mentor Graphics, a U.S.-based company. Prior to that, he held research and development roles in the Chinese Academy of Sciences. Prior to March 2011, Mr. Pan was an independent director of Beijing Lanxum Technology Co. Ltd., a Chinese A-share listed company. Mr. Pan holds a master's degree and a bachelor's degree in engineering from Tsinghua University in Beijing, and an Executive Master of Business Administration degree from China-Europe International Business School.

*Eric Zhe XU* has been an independent director of our company since December 2012. Mr. Xu is a Chartered Financial Analyst and currently serves as a managing director for the China Aerospace Industry Investment Fund. From October 2005 to October 2010, Mr. Xu served as a principal at SAIF Partners and, prior to that, as a consultant at Boston Consulting Group and an associate at A.T. Kearney Inc. Mr. Xu holds a Master of Business Administration degree from Harvard Business School and a bachelor's degree in economics from Peking University.

*Chaoyang XIA* has been an independent director of our company since March 2010. Dr. Xia is a founding partner of Tianjin Ivy Investment Management Center (Limited Partnership), a venture capital and growth equity firm in China. He is also a founding partner of Shanghai Ivy Investment Management Center (Limited Partnership). He has been chairman of Benxian Investment (Beijing) Ltd. since May 2008 and an independent director of Tellhow Sci-Tech Co., Ltd., a company listed on the Shanghai Stock Exchange, since September 2012. He also served as a director of China Newstar Energy Co., Ltd. from 2009 to 2012. From 2001 to 2008, he was chief financial officer and senior vice president of CapitalBio Corporation, a leading biochip company in the PRC. Before joining CapitalBio Corporation, Dr. Xia served as a General Manager of the Investment Department of Tsinghua Tongfang Co., Ltd., a technology company listed on the Shanghai Stock Exchange. Prior to that, Dr. Xia was a deputy general manager of the Investment Banking Division of CITIC Securities Company Limited. Dr. Xia holds a doctorate degree in engineering, a bachelor's degree in engineering and a bachelor's degree in economics, all from Tsinghua University.

*Songzuo XIANG* has been an independent director of our company since September 2008. Dr. Xiang is the editor-in-chief of the Global Business & Finance magazine, a Chinese business publication sponsored by the Development Research Center of the State Council. He has also been appointed as the chief economist of the Agricultural Bank of China Limited since March 2012. Dr. Xiang is currently a director of AirMedia Group Inc., a company listed on the Nasdaq Global Market. Dr. Xiang was also a director of Hurray! Solutions Ltd. from 2000 to 2009 and its chief executive officer from March to October 2009, respectively. From 1995 to 1998, Dr. Xiang was deputy director of the Fund Planning Department at the Shenzhen branch office of the People's Bank of China. Dr. Xiang holds a master's degree in international affairs from Columbia University, a doctorate degree and a master's degree in economics from Renmin University of China and a bachelor's degree in mechanical engineering from Huazhong University of Science and Technology.

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## **Table of Contents**

*Zhenwen LIANG* has served as the chief financial officer of our company since November 2010. Mr. Liang has served as general manager of the Company's new business unit, responsible for developing value-added services, since 2006. From 2004 to 2006, Mr. Liang was responsible for overseeing our entire financial operations. From 1998 to 2004, Mr. Liang headed the finance team at N-T Information Engineering. Mr. Liang has a bachelor's degree in accounting from the Central University of Finance and Economics and a master's degree in business administration from Renmin University of China. Mr. Liang is a member of the Chinese Institute of Certified Public Accountants.

*Dong LI* has served as our president since March 2009 and as the chief marketing officer of our company since our establishment in 2004. From 2001 to 2004, he was the assistant to the general manager and chief marketing officer of N-T Information Engineering. He previously worked at China Technology Import and Export Corp. Mr. Li holds a bachelor's degree in materials science and technology from Tsinghua University.

*Tianxing WANG* has served as the chief technology officer of our company since September 2012. Mr. Wang has served as our chief scientist since 2007. From 1998 to 2007 he served as our director of software technology, overseeing the design and development of our CA products. Mr. Wang holds a master's degree and a bachelor's degree in computer science and technology from Tsinghua University.

*Huiqing CHEN* has served as the chief administrative officer of our company since our establishment in 2004, and is responsible for administrative affairs and human resources management. From 1998 until 2004, she was manager of the general manager's office at N-T Information Engineering. Ms. Chen holds a master's degree in biochemical engineering from Tsinghua University.

Each of James Hsiang Ming HO and Chaoyang XIA was re-elected as a director at our annual general meeting of shareholders held on December 21, 2012. Ching Wah Ng, formerly an independent director, resigned from our board of directors on December 31, 2012 due to personal reasons. On the same date, Eric Zhe Xu was appointed as an independent director.

There is no family relationship among any of our directors or executive officers. There is no shareholding qualification for directors.

## **B. Compensation of Directors and Senior Officers**

Our executive officers receive compensation in the form of salaries, annual bonuses and share options. Some of our current and former directors have received compensation in the form of share options. We do not provide any benefits to our non-executive directors upon retirement. In 2012, the aggregate cash compensation to our directors and executive officers was US\$1.3 million.

### **Share Options**

Our Amended and Restated China Digital TV Holding Co., Ltd. 2005 Stock Incentive Plan, or the 2005 Stock Incentive Plan, China Digital TV Holding Co., Ltd. 2008 Stock Incentive Plan, or the 2008 Stock Incentive Plan, China Digital TV Holding Co., Ltd. 2010 Stock Incentive Plan, or the 2010 Stock Incentive Plan, and China Digital TV Holding Co., Ltd. 2012 Stock Incentive Plan, or the 2012 Stock Incentive Plan, are intended to provide incentives to our directors, officers and employees as well as consultants and advisers of our company and its present or future parent company or subsidiaries, or the related corporations.

### ***The 2005 Stock Incentive Plan***

The 2005 Stock Incentive Plan was adopted by the board of directors of CDTV BVI on February 3, 2005 and the Amended and Restated 2005 Stock Incentive Plan was adopted by our board of directors and approved by our shareholders on September 13, 2007 to amend and restate the 2005 Stock Incentive Plan. In 2005, CDTV BVI was the ultimate holding company of our business. As a result of our restructuring in May 2007, CDTV BVI became our wholly-owned subsidiary and the options already granted under the 2005 Stock Incentive Plan were converted to options for the ordinary shares of our company. Pursuant to the 2005 Stock Incentive Plan, we may issue share options, stock appreciation rights, share bonuses, restricted shares, performance shares, share units, phantom shares, dividend equivalents or similar rights to purchase or acquire shares.

## **Table of Contents**

We reserved a total of 4,444,440 ordinary shares for issuance under the 2005 Stock Incentive Plan, subject to any adjustments as contemplated by the plan. We granted share options to purchase 3,067,498, 47,918, 543,674, 620,212 and 53,280 ordinary shares pursuant to the 2005 Stock Incentive Plan on February 3, 2005, April 13, 2006, September 22, 2006, December 5, 2006 and October 5, 2008, respectively. On November 19, 2010, the number of ordinary shares reserved for issuance under the 2005 Stock Incentive Plan was cancelled to the extent the corresponding options had not been awarded as of that date. Options to purchase 20,809 ordinary shares remained outstanding as of March 31, 2013 under the 2005 Stock Incentive Plan.

With respect to the share options that we granted on February 3, 2005, two vesting schedules apply. The first vesting schedule is as follows: 50% vest at the end of the six-month period after the award date, and the remaining 50% vest in 42 equal monthly installments, beginning from the end of the six-month period after the award date. The second vesting schedule is as follows: 25% vest on the first anniversary of the award date and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The original exercise price for all share options granted on this date was US\$0.543 per share.

With respect to the share options that we granted on April 13, 2006, the vesting schedule is as follows: 50% vest at the end of the six-month period after the award date, and the remaining 50% vest in 42 equal monthly installments, beginning from the end of the six-month period after the award date. The original exercise price for all share options granted on this date was US\$0.543 per share.

With respect to the share options that we granted on September 22, 2006, the vesting schedule is as follows: 25% vest on the first anniversary of the award date and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The original exercise price was US\$1.771 per share.

With respect to the share options that we granted on December 5, 2006, with the exception of share options that we granted to one of our executive officers, the vesting schedule is as follows: 25% vest on the first anniversary of the award date, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The executive officer's share options vest according to the following schedule: 25% of 320,000 options vest upon the closing of our initial public offering; 75% of 320,000 options vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the executive officer took office; and 32,000 options vest upon the achievement of certain financial targets. In July 2010, these 32,000 shares were forfeited as the financial targets were not met. The original exercise price for all share options granted on this date was US\$4.172.

With respect to the share options that we granted on October 5, 2008, the vesting schedule is as follows: 25% vest on the first anniversary of the award date and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The original exercise price was US\$0.543 per share.

### ***2008 Stock Incentive Plan***

The 2008 Stock Incentive Plan was adopted by our board of directors and approved by our shareholders on September 13, 2007. Pursuant to the 2008 Stock Incentive Plan, we may issue share options, share appreciation rights, share bonuses, restricted shares and restricted share units, performance shares, share units, phantom shares, dividend equivalents or similar rights to purchase or acquire shares.

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**Table of Contents**

We reserved a total of 1,200,000 ordinary shares for issuance under the 2008 Stock Incentive Plan, subject to any adjustments as contemplated by the plan. The plan also provides for an annual increase, beginning in 2009, in the number of ordinary shares that may be delivered pursuant to awards under the plan, totaling 2% of our issued and outstanding shares as of the first business day of the relevant calendar year. The maximum number of shares subject to awards that may be granted during any single calendar year is such number as equals 2% of our issued and outstanding shares as of the first business day of that calendar year. We granted share options to purchase 406,776, 357,548, 42,880 and 50,000 ordinary shares on October 5, 2008, June 2, 2009, February 10, 2010 and November 15, 2010, respectively. On November 19, 2010, the number of ordinary shares that had been reserved for issuance under the 2008 Stock Incentive Plan was cancelled to the extent the corresponding options had not been awarded as of that date. Options to purchase 589,478 ordinary shares remained outstanding as of March 31, 2013 under the 2008 Stock Incentive Plan.

With respect to the share options that we granted on October 5, 2008, the vesting schedule is as follows: 25% vest on the first anniversary of the award date, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The original exercise price was US\$7.89 per share. On February 10, 2010, we accelerated the vesting schedule of a total of 29,480 share options to purchase 29,480 ordinary shares so that all these share options were vested on February 20, 2010.

With respect to the share options that we granted on June 2, 2009, the vesting schedule is as follows: 25% vest on the first anniversary of the award date, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The original exercise price was US\$9.09 per share.

With respect to the share options that we granted on February 10, 2010, all these share options were vested on the grant date. The original exercise price was US\$0.543 per share.

With respect to the share options that we granted on November 15, 2010, the vesting of these options is conditional upon the fulfillment of certain performance targets by the optionee in the four years following the grant date. The original exercise price was US\$6.96 per share.

***2010 Stock Incentive Plan***

The 2010 Stock Incentive Plan was adopted by our board of directors on November 19, 2010. Pursuant to the 2010 Stock Incentive Plan, we may issue share options, share appreciation rights, share bonuses, restricted shares, performance shares, share units, phantom shares, dividend equivalents or similar rights to purchase or acquire shares.

We reserved a total of 3,600,000 ordinary shares for issuance under the 2010 Stock Incentive Plan, subject to adjustments as contemplated by the plan. We granted share options to purchase 1,000,000, 1,600,000, 700,000 and 300,000 ordinary shares on November 19, 2010, May 16, 2011, September 30, 2011 and November 19, 2011, respectively. Options to purchase 3,504,675 ordinary shares remained outstanding as of March 31, 2013 under the 2010 Stock Incentive Plan.

With respect to the share options that we granted on November 19, 2010, the vesting schedule is as follows: 25% vest on the first anniversary of the award date, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on the last day of the month following the month in which the first anniversary of the award date occurs. The original exercise price was US\$6.90 per share.

With respect to the share options that we granted on May 16, 2011, two vesting schedules apply. The first vesting schedule is as follows: 25% vest on November 19, 2011, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on December 31, 2011 and then on the last day of the month following thereafter. The second vesting schedule is as follows: the vesting of the options is conditioned upon the fulfillment of certain performance targets by the optionees on April 1, 2012. The original exercise price was US\$4.90 per share.

With respect to the share options that we granted on September 30, 2011, the vesting schedule is as follows: 25% vest on November 19, 2011, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on December 31, 2011 and then on the last day of the month following thereafter. The exercise price is US\$4.34 per share.

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## **Table of Contents**

With respect to the share options that we granted on November 19, 2011, the vesting schedule is as follows: 25% vest on November 19, 2011, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on December 31, 2011 and then on the last day of the month following thereafter. The exercise price is US\$4.34 per share.

### ***2012 Stock Incentive Plan***

The 2012 Stock Incentive Plan was adopted by our board of directors on May 1, 2012. Pursuant to the 2012 Stock Incentive Plan, we may issue share options, share appreciation rights, share bonuses, restricted shares, performance shares, share units, phantom shares, dividend equivalents or similar rights to purchase or acquire shares.

We reserved a total of 1,200,000 ordinary shares for issuance under the 2012 Stock Incentive Plan, subject to adjustments as contemplated by the plan. We granted share options to purchase 1,200,000 ordinary shares on January 8, 2013. Options to purchase 1,188,979 ordinary shares remained outstanding as of March 31, 2013 under the 2012 Stock Incentive Plan.

With respect to the share options that we granted on January 8, 2013, the vesting schedule is as follows: 25% vest on January 8, 2013, and the remaining 75% vest in 36 substantially equal monthly installments, beginning on February 28, 2013 and then on the last day of the month following thereafter. The exercise price is US\$1.18 per share.

### ***The 2005, 2008, 2010 and 2012 Stock Incentive Plans***

Our board of directors administers the 2005 and 2008 Stock Incentive Plans and Jianhua Zhu administers the 2010 and 2012 Stock Incentive Plans. The administrator of each plan has wide discretion in determining who will receive awards, the type and timing of awards, the vesting schedule and other terms and conditions of the awards, including the exercise price of share option grants. Generally, if an outstanding share option grant made under the plans has not vested by the date of termination of the recipient's employment with us, no further installments of the recipient's grant will become exercisable following the date of termination of employment, and the recipient will have 30 days from such date to exercise any share options that had already vested but not yet been exercised. If any ordinary shares subject to a restricted share award remain subject to restrictions by the date of termination of employment, no additional ordinary shares will vest following the date of termination of employment.

Our board of directors may amend or terminate the 2005, 2008, 2010 and 2012 Stock Incentive Plans at any time; provided, however, that our board of directors must seek the recipients' approval with respect to any amendment or termination that would adversely affect the rights of such recipients under any award already made. Without further action by our board of directors, the 2005, 2008, 2010 and 2012 Stock Incentive Plans will terminate on February 2, 2015, September 12, 2017, November 18, 2020 and April 30, 2022, respectively.

In addition to the options granted pursuant to the 2005, 2008, 2010 and 2012 Stock Incentive Plans, on May 15, 2007, we granted options to purchase 40,000 ordinary shares to Louis T. Hsieh, who became an independent director of our company upon the completion of our initial public offering, at an exercise price of US\$4.172 per share. Mr. Hsieh retired from our board of directors in December 2009, following which 33,889 of his options were exercised with the remainder being forfeited.

On November 19, 2010, our board of directors approved an adjustment to the exercise price of all options granted prior to, but remained outstanding as of December 23, 2010 under the 2005 Stock Incentive Plan, the 2008 Stock Incentive Plan and the 2010 Stock Incentive Plan, or the Adjusted Options. The per share exercise price of all Adjusted Options with a per share exercise price higher than US\$2.00 was reduced by US\$2.00 on December 23, 2010, and the per share exercise price of all Adjusted Options with a per share exercise price no more than US\$2.00 was reduced to US\$0.01. Our board of directors also resolved that if any future dividend is declared, the per share exercise price of all options granted prior to and outstanding as of the date of record of such dividend shall be reduced by an amount equal to the dividend payable on each ordinary share, provided that the per share exercise price after adjustment shall not be less than US\$0.01. Due to special cash dividends of US\$0.56 and US\$2.30 per ordinary share declared in May 2011 and November 2012, respectively, the per share exercise prices of all of the options granted prior to and remaining outstanding as of June 20, 2011 and those as of November 26, 2012, the record dates, were reduced by US\$0.56 and US\$2.30 pursuant to such resolution of our board of directors referenced above, respectively, provided that the per share exercise prices after adjustment shall not be less than US\$0.01.

**Table of Contents**

The following table sets forth information on share options that have been granted and were outstanding as of March 31, 2013 pursuant to the 2005, 2008, 2010 and 2012 Stock Incentive Plan:

|  | Number of Ordinary Shares Underlying Outstanding Options | Exercise Price per Ordinary Share** | Date of Grant      | Date of Expiration |
|--|--|-------------------------------------|--------------------|--------------------|
| <b>Directors and Executive Officers</b>                |  |                                     |                    |                    |
| Jianhua ZHU  | 1,150,000  | US\$ 2.04                           | November 19, 2010  | November 19, 2020  |
|  |  | US\$ 1.18                           | January 8, 2013    | January 7, 2023    |
| Zengxiang LU   | 1,150,000  | US\$ 2.04                           | May 16, 2011       | May 15, 2021       |
|  |  | US\$ 1.18                           | January 8, 2013    | January 7, 2023    |
| Zhenwen LIANG  | *  | US\$ 2.04                           | September 30, 2011 | September 29, 2021 |
|  |  | US\$ 1.18                           | January 8, 2013    | January 7, 2023    |
| Dong LI  | *  | US\$ 4.23                           | June 2, 2009       | June 1, 2019       |
|  |  | US\$ 3.03                           | October 5, 2008    | October 4, 2018    |
|  |  | US\$ 2.04                           | September 30, 2011 | September 29, 2021 |
|  |  | US\$ 1.18                           | January 8, 2013    | January 7, 2023    |
| Tianxing WANG  | *  | US\$ 4.23                           | June 2, 2009       | June 1, 2019       |
|  |  | US\$ 3.03                           | October 5, 2008    | October 4, 2018    |
|  |  | US\$ 2.04                           | May 16, 2011       | May 15, 2021       |
|  |  | US\$ 2.04                           | November 19, 2011  | November 18, 2021  |
|  |  | US\$ 1.18                           | January 8, 2013    | January 7, 2023    |
| Huiqing CHEN   | *  | US\$ 4.23                           | June 2, 2009       | June 1, 2019       |
|  |  | US\$ 3.03                           | October 5, 2008    | October 4, 2018    |
|  |  | US\$ 2.04                           | September 30, 2011 | September 29, 2021 |
|  |  | US\$ 1.18                           | January 8, 2013    | January 7, 2023    |
| <b>Other Grantees</b>                                  |  |                                     |                    |                    |
| Other grantees as a group (comprising 157 individuals) | 2,071,060  |                                     |                    |                    |

\* The number of ordinary shares underlying the outstanding options held by each of the officers represents less than 1% of our ordinary shares.

\*\* The exercise price per Ordinary Share has reflected the impact of the exercise price modifications in December 2010, June 2011 and November 2012, respectively.

**C. Board Practices****General**

The functions and powers of our board of directors include, among others:

convening shareholders' annual general meetings and reporting its work to shareholders at such meetings;

implementing shareholders' resolutions;

determining our business plans and investment proposals;

declaring dividends and distributions;

exercising the borrowing powers of our company and mortgaging the property of our company;

approving the transfer of shares of our company, including the registering of such shares in our share register; and

## **Table of Contents**

exercising any other powers conferred by the shareholders meetings or under our Second Amended and Restated Memorandum and Articles of Association.

### **Terms of Directors**

Our Second Amended and Restated Memorandum and Articles of Association provide for three classes of directors, each with three-year terms. The term of the Class I directors, who are Dr. Zengxiang Lu and Jianhua Zhu, will expire upon the annual general meeting of shareholders to be held in 2014; the term of the Class II directors, who are James Hsiang Ming Ho and Dr. Chaoyang Xia, will expire upon the annual general meeting of shareholders to be held in 2015; and the term of the Class III directors, who are Jianyue Pan, Songzuo Xiang and Eric Zhe Xu, will expire upon the annual general meeting of shareholders to be held in 2013.

### **Employment Agreements**

We have entered into service contracts with our directors. The service contracts do not provide any benefits to our directors upon termination of service.

We have entered into an employment agreement with each of our executive officers. Under these agreements, we may terminate an executive officer's employment for cause at any time, without notice or remuneration, for certain acts of the executive officer, including but not limited to material acts of fraud, material violations of our terms of employment, material dereliction of duty or engaging in graft to the material harm of the company. An executive officer may terminate employment if a government regulatory agency determines that working conditions are extremely deficient and injurious to health, if the executive has been subject to violence, threats or illegal constraints upon his liberty, or if we have failed to pay compensation on time. We and each executive officer may also decide to terminate such executive officer's employment for other reasons or no reason after providing written notice at least 30 days in advance and after we have made arrangements for a successor. Our employment agreements do not provide any benefits to any of our executive officers upon termination.

Each executive officer who has executed an employment agreement with us has agreed to hold in confidence and not to use, both during and after such executive officer's term of employment, any of our confidential information, including but not limited to information relating to important company policies, technological secrets, commercial secrets, company processes and any intellectual property discovered, invented or created by such executive officer during his or her term of employment. In addition, each of our executive officers has agreed to give us full rights to any work-related patents, inventions or achievements.

Each executive officer also has agreed that for one year after terminating employment with us, such executive officer will not, without our consent, accept employment by any of our competitors or engage in any activities that, directly or indirectly, compete with us. In addition, each executive officer has agreed that he or she will not, without our consent, induce any of our employees to terminate employment with us.

### **Board Committees**

To enhance our corporate governance, our board of directors established three board committees: an audit committee, a corporate governance and nominations committee and a compensation committee. The charters of each of our audit committee, corporate governance and nominations committee and compensation committee are publicly available on our website at <http://ir.chinadtv.cn>.

#### ***Audit Committee***

Our audit committee is responsible for, among other things:

recommending to our shareholders, if appropriate, the annual reappointment of our independent auditors and pre-approving all audit and non-audit services permitted to be performed by our independent auditors;

## **Table of Contents**

annually reviewing with our independent auditors any audit problems or difficulties and management's response;

reviewing and approving all proposed related-party transactions, as defined in Item 404 of Regulation S-K promulgated by the SEC;

discussing the annual audited financial statements with management and our independent auditors;

discussing with management and the independent auditors major issues regarding accounting principles and financial statement presentations;

reviewing major issues as to the adequacy of our internal controls and any special audit steps adopted in light of material control deficiencies;

discussing policies with respect to risk assessment and risk management;

timely reviewing reports from the independent auditors regarding all critical accounting policies and practices to be used by our company, all alternative treatments of financial information within U.S. GAAP that have been discussed with management and all other material written communications between the independent auditors and management;

establishing procedures for the receipt, retention and treatment of complaints received by us regarding accounting, internal accounting controls or auditing matters, and for the confidential, anonymous submission by our employees of concerns regarding questionable accounting or auditing matters;

annually reviewing and reassessing the adequacy of our audit committee charter;

meeting separately and periodically with management and our internal and independent auditors; and

reporting regularly to our board of directors.

Our audit committee currently consists of Songzuo Xiang, Jianyue Pan and Chaoyang Xia, and has a formal written charter that sets forth its duties and powers. Our board has determined that each of Songzuo Xiang, Jianyue Pan and Chaoyang Xia qualifies as an independent director under the rules of the SEC and the NYSE. Our board also has determined that Songzuo Xiang qualifies as an audit committee financial expert within the meaning of the rules of the SEC. Our audit committee meets at least once each quarter.

### ***Corporate Governance and Nominations Committee***

Our corporate governance and nominations committee consists of Songzuo Xiang, Jianyue Pan and Chaoyang Xia, and has a formal written charter that sets forth its duties and powers. Our corporate governance and nominations committee is responsible for identifying individuals qualified to become members of our board of directors and recommending them to our board of directors for nomination. Our corporate governance and nominations committee is also responsible for implementing our Code of Business Conduct and Ethics.

### ***Compensation Committee***

Our compensation committee currently consists of Songzuo Xiang and Chaoyang Xia, and has a formal written charter that sets forth its duties and powers. Our compensation committee assists the board in reviewing and approving our compensation structure, including all forms of

compensation relating to our directors and executive officers, and administering our stock incentive plans.

**Table of Contents****Corporate Governance Guidelines**

Our board of directors has adopted a set of corporate governance guidelines. These guidelines reflect certain guiding principles with respect to the composition, selection and performance evaluation of our board of directors, the board committees, management succession and executive compensation. They are publicly available on our website at <http://ir.chinadtv.cn>.

**D. Employees**

See Item 4. Information on the Company B. Business Overview Employees.

**E. Share Ownership**

Under the Exchange Act Rule 13d-3, a person is deemed to be a beneficial owner of a security if that person has or shares voting power, which includes the power to vote or to direct the voting of such security, or investment power, which includes the power to dispose of or to direct the disposition of such security. A person is also deemed to be the beneficial owner of any securities of which that person has a right to acquire beneficial ownership within 60 days. Under these rules, more than one person may be deemed a beneficial owner of securities as to which such person has no economic interest.

The following table sets forth certain information with respect to the directors, officers and each of the persons known to us who own beneficially 5% or more of our ordinary shares as of March 31, 2013 unless otherwise indicated. The number of ordinary shares outstanding in calculating the percentages for each listed person includes the ordinary shares underlying share options held by such person. The percentage of beneficial ownership of each listed person is based on 59,101,566 ordinary shares outstanding (excluding the 421,526 ordinary shares that were issued and held for the Company's account in preparation for exercise of share options by option holders under our employee stock incentive plans), as well as the ordinary shares underlying share options exercisable by such person within 60 days of March 31, 2013.

|  | Shares beneficially owned |         |
|--|---------------------------|---------|
|  | Number                    | Percent |
| <b>Directors and Executive Officers</b>                    |                           |         |
| Jianhua ZHU <sup>(1)</sup>                                 | 3,501,746                 | 5.9%    |
| Zengxiang LU <sup>(2)</sup>                                | 3,501,746                 | 5.9%    |
| James Hsiang Ming HO                                       |                           |         |
| Jianyue PAN  | *                         | *       |
| Songzuo XIANG  |                           |         |
| Chaoyang XIA   |                           |         |
| Eric Zhe XU  |                           |         |
| Zhenwen LIANG <sup>(3)</sup>                               | **                        | **      |
| Dong LI <sup>(4)</sup>                                     | **                        | **      |
| Tianxing WANG <sup>(5)</sup>                               | **                        | **      |
| Huiqing CHEN <sup>(6)</sup>                                | **                        | **      |
| Directors and executive officers as a group <sup>(7)</sup> | 8,232,223                 | 13.8%   |
| <b>Principal Shareholders</b>                              |                           |         |
| Yuk Shing WONG <sup>(8)</sup>                              | 4,396,832                 | 7.4%    |
| Capital Funds <sup>(9)</sup>                               | 12,000,000                | 20.3%   |
| SAIF <sup>(10)</sup>                                       | 11,885,820                | 20.1%   |

\* Beneficially owns less than 1% of our ordinary shares.

\*\* Upon exercise of all share options exercisable within 60 days of March 31, 2013, would beneficially own less than 1% of our ordinary shares.

**Table of Contents**

- (1) Represents: (i) the 2,663,393 ordinary shares held by Smart Live Group Limited, which is wholly owned by Jianhua Zhu; (ii) the 326,704 ordinary shares held by China Cast Investment Holdings Limited, or China Cast; and (iii) the 675,001 ordinary shares issuable upon exercise of options held by Mr. Zhu that are exercisable within 60 days of March 31, 2013. Mr. Zhu, together with Dr. Zengxiang Lu, exercises investment and voting powers over these shares held by China Cast. Mr. Zhu owns 50% of the equity interest of China Cast and disclaims beneficial ownership of those shares held by China Cast except to the extent of his pecuniary interest therein.
- (2) Represents: (i) the 2,663,393 ordinary shares held by Polar Light Group Limited, which is wholly owned by Dr. Zengxiang Lu; (ii) the 326,704 ordinary shares held by China Cast; and (iii) the 675,001 ordinary shares issuable upon exercise of options held by Dr. Lu that are exercisable within 60 days of March 31, 2013. Dr. Lu, together with Jianhua Zhu, exercises investment and voting powers over these shares held by China Cast. Dr. Lu owns 50% of the equity interest of China Cast and disclaims beneficial ownership of those shares held by China Cast except to the extent of his pecuniary interest therein.
- (3) Represents the sum of ordinary shares owned by Mr. Liang and ordinary shares issuable upon exercise of options held by Mr. Liang.
- (4) Represents the sum of ordinary shares owned by Mr. Li and ordinary shares issuable upon exercise of options held by Mr. Li.
- (5) Represents the sum of ordinary shares owned by Mr. Wang and ordinary shares issuable upon exercise of options held by Mr. Wang.
- (6) Represents the sum of ordinary shares owned by Ms. Chen and ordinary shares issuable upon exercise of options held by Ms. Chen.
- (7) Represents 100% of the 326,704 ordinary shares held by China Cast (Jianhua Zhu and Dr. Zengxiang Lu jointly exercise investment and voting powers over the shares held by China Cast), ordinary shares held by Mr. Zhu (other than those ordinary shares held through China Cast), Dr. Lu (other than those ordinary shares held through China Cast), Mr. Liang, Mr. Li, Mr. Wang, Ms. Chen and Mr. Pan and ordinary shares issuable upon exercise of options held by Mr. Zhu, Dr. Lu, Mr. Liang, Mr. Li, Mr. Wang and Ms. Chen.
- (8) Represents the sum of ADSs owned by Yuk Shing Wong.
- (9) Includes 11,613,600 and 386,400 ordinary shares held by Capital International Private Equity Fund IV, L.P. and CGPE IV, L.P., respectively. Each of Capital International Private Equity Fund IV, L.P. and CGPE IV, L.P. is a limited partnership established in the State of Delaware, United States. The address of each of the Capital Funds is 6455 Irvine Center Drive, Irvine, California 92618, U.S.A. The general partner of Capital International Private Equity Fund IV, L.P. is Capital International Investments IV, L.P. The general partner of Capital International Investments IV, L.P. is Capital International Investments IV, LLC, which is also the general partner of CGPE IV, L.P. Capital International Inc. is the investment manager of Capital International Private Equity Fund IV, L.P. as well as the managing member of Capital International Investments IV, LLC. Capital International, Inc. is a wholly-owned subsidiary of Capital Group International, Inc. and a wholly-owned indirect subsidiary of The Capital Group Companies, Inc.
- (10) Represents the ordinary shares held by SAIF. SAIF is a limited partnership organized in the Cayman Islands and has the following address: c/o Maples and Calder, Ugland House, P.O. Box 309, George Town, Grand Cayman, Cayman Islands. SB Asia Pacific Partners L.P., or the GP, is the sole general partner of SAIF. SB Asia Pacific Investments Limited, or SB Investments, is the sole general partner of the GP. Asia Infrastructure Investments Limited, or Asia Investments, is the sole shareholder of SB Investments. Asia Investments is controlled, in respect of its authority over SB Investments, by SB First Singapore Pte. Ltd., or SB Singapore. SOFTBANK Corporation is the sole shareholder of SB Singapore. Mr. Ronald D. Fisher is the sole director of SB Investments.

**Item 7. Major Shareholders and Related Party Transactions**

**A. Major Shareholders**

Please refer to Item 6. Directors, Senior Management and Employees E. Share Ownership in this annual report.

None of our major shareholders has voting rights different from those of our other shareholders. To the best of our knowledge, we are not directly or indirectly controlled by another corporation, by any foreign government or by any other natural or legal person severally or jointly.

We are not aware of any arrangement that may, at a subsequent date, result in a change of control of our company.

For information regarding our shares held or beneficially owned by persons in the United States, see Item 9. The Offer and Listing A. Offering and Listing Details Market and Share Price Information in this annual report.

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## **Table of Contents**

### **B. Related Party Transactions**

#### **Super TV and N-S Digital TV Arrangements**

We operate our business in the PRC through N-S Digital TV, a PRC company owned by PRC citizens. We do not own any equity interest in N-S Digital TV. Through Super TV, our indirectly wholly-owned subsidiary in the PRC, we have entered into a series of contractual arrangements with N-S Digital TV and its shareholders, including contracts relating to transfer of assets, supply of smart cards and related software products, provision of equipment and technical support and related services, technology development and licenses, and certain shareholder rights and corporate governance matters. In addition, N-S Digital TV and N-T Information Engineering have entered into certain agreements relating to transfer of assets, assignment of intellectual property rights and equity interests.

The following is a summary of the material provisions of certain of these agreements. For more complete information you should read these agreements in their entirety.

#### ***Transfer of Assets and Equity Interests and Intellectual Property Rights***

***Equity Transfer Agreement, dated August 4, 2006, between N-T Information Engineering and N-S Digital TV.*** N-T Information Engineering agreed to transfer to N-S Digital TV its 51% equity interest in Guokai for a consideration of RMB2.4 million (US\$0.3 million), which was subsequently reduced to RMB2.3 million (US\$0.3 million) by an agreement among N-S Digital TV, N-T Information Engineering and the other shareholder of Guokai. This transaction was approved by the relevant PRC governmental authorities and completed on July 27, 2007.

***Asset Transfer Agreement, dated August 5, 2006, between N-T Information Engineering and N-S Digital TV, as amended on April 6, 2007.*** N-T Information Engineering transferred its set-top box-related assets and employees to N-S Digital TV for an initial purchase price of RMB29.4 million (US\$3.8 million). The initial purchase price is subject to an adjustment mechanism that will require N-T Information Engineering to refund to N-S Digital TV: (i) the difference between the initial purchase price and the first adjustment price, defined as ten times the total sales receipts during the period from August 1, 2006 through December 31, 2006 with respect to the transferred set-top box business, if such difference is a positive number; and (ii) the difference between the initial purchase price and the second adjustment price, defined as six times the net profit of the transferred set-top box business for the year ending December 31, 2007, if the initial purchase price is greater than the second adjustment price. The net profit of the transferred set-top box business for the year ending December 31, 2007 is required to be reviewed by a big-four accounting firm. As an adjustment to the initial purchase price, N-T Information Engineering refunded US\$1.5 million to N-S Digital TV in April 2007. In November 2007, N-S Digital TV waived the remaining amount that may be payable by N-T Information Engineering to Super TV under the adjustment mechanism. N-T Information Engineering covenanted not to engage in any business activities in the PRC or outside of the PRC that directly or indirectly are in competition with the business transferred to N-S Digital TV under this agreement.

***Fixed-assets Transfer Agreement, dated March 28, 2007, between N-S Digital TV and Super TV.*** Super TV sold to N-S Digital TV certain fixed assets relating to its digital television business for a cash consideration of RMB0.8 million (US\$0.1 million).

***Trademark Licensing Agreement entered into between N-T Information Engineering and N-S Digital TV in March 2007 and Transfer of a Graphic Logo by N-T Information Engineering to N-S Digital TV in December 2008.*** N-T Information Engineering granted N-S Digital TV a non-exclusive license to use certain trademarks free of charge. In December 2008, N-T Information Engineering transferred to Super TV, free of charge, the trademark for the graphic logo that was previously licensed to N-S Digital TV under this agreement. For details of this licensing agreement and the transfer of the trademark for the graphic logo, see Item 4. Information on the Company B. Business Overview Intellectual Property.

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**Table of Contents**

**Intellectual Property Rights Transfer Agreement, dated August 13, 2008, between N-T Information Engineering and Super TV.** N-T Information Engineering transferred all of its intellectual property rights relating to the digital watermarking and image tracing technologies to Super TV, including one patent issued and five pending patent applications in the PRC. The transfer price is RMB21.2 million (US\$3.1 million), which was fully paid by Super TV in September 2008. See Item 4. Information on the Company B. Business Overview Intellectual Property. A portion of the transfer price under this agreement in the amount of RMB8.8 million (US\$1.3 million) was attributable to the acquisition of the intellectual property rights relating to the digital watermarking and image tracing technologies and the remainder was reallocated to the acquisition of N-T Information Engineering's equity interest in N-S Digital TV by two of our employees.

**Technical Support, Smart Cards and Software, Licenses and Equipment**

**Technical Support and Related Services Agreement, dated June 7, 2004 and amended on February 9, 2012, between N-S Digital TV and Super TV.** Super TV exclusively provides N-S Digital TV and/or its customers with technical support, technical training, personnel services relating to N-S Digital TV's marketing activities and services relating to the maintenance and optimization for the products and software of N-S Digital TV's customers at N-S Digital TV's request. The fees for such technical support and services are determined at Super TV's discretion and payable within five days after the delivery of the support and services or at any other time agreed to by the parties. The value of the transactions between N-S Digital TV and Super TV under this agreement was RMB11.2 million (US\$1.8 million) in 2012. The term of this agreement is 15 years, which may not be terminated prior to its termination date without Super TV's written consent. The term of this agreement will be automatically renewed for an additional 15 years upon its termination date, unless written notice has been given by Super TV.

**Technology License Agreement, dated June 7, 2004 and amended on February 9, 2012, between N-S Digital TV and Super TV.** N-S Digital TV granted Super TV, free of charge, an exclusive license to use certain software copyrights, patents, unpatentable technology and technical secrets relating to the digital television business that was transferred from N-T Information Engineering to N-S Digital TV. The term of the license is ten years. This agreement may not be terminated or amended without the written consent of Super TV prior to its termination date and will be automatically renewed for an additional ten years upon its termination date, unless written notice has been given by Super TV.

**Technology Development Agreement, dated June 7, 2004 and amended on February 9, 2012, between N-S Digital TV and Super TV.** N-S Digital TV engaged Super TV to develop all technology required by N-S Digital TV or its customers. The fees payable by N-S Digital TV to Super TV under the agreement will be calculated according to the following formula:

The price at which N-S Digital TV sells the technology products developed by Super TV multiplied by a set percentage multiplied by the quantity of the products sold.

The set percentage is determined by Super TV. In 2012, N-S Digital TV paid nil to Super TV under this agreement. The term of the agreement is ten years, which may not be terminated prior to its termination date without Super TV's written consent. The term of this agreement will be automatically renewed for an additional ten years upon its termination date, unless written notice has been given by Super TV.

**Products and Software Purchase Agreement, dated June 7, 2004 and amended on February 9, 2012, between N-S Digital TV and Super TV.** N-S Digital TV agreed to exclusively purchase from Super TV all the smart cards and related software products required for its CA systems. The purchase price was RMB65 (US\$9.5) for each smart card (including related software), which is determined by Super TV and may be adjusted annually by Super TV based on fair market value. The term of the agreement is 15 years, which may not be terminated prior to its termination date without Super TV's written consent. The term of this agreement will be automatically renewed for another 15 years upon its termination date, unless written notice has been given by Super TV. N-S Digital TV subsequently obtained Super TV's consent to produce by itself or purchase from a third party smart cards beginning March 2006. The aggregate value of transactions between N-S Digital TV and Super TV under this agreement was RMB332.6 million (US\$52.7 million) in 2012.

**Table of Contents**

***Framework Agreement for Purchase of Computer Chips, dated December 12, 2008, between N-S Digital TV and Super TV.*** Pursuant to this agreement, N-S Digital TV will purchase computer chips from Super TV, which in turn will source such computer chips from suppliers such as STM and Infineon. The term of this agreement is indefinite and is terminable by agreement between the parties. The aggregate value of transactions between N-S Digital TV and Super TV under this agreement was RMB6.2 million (US\$1.0 million) in 2012.

***Framework Agreement for Sale of Software Products, dated July 14, 2009, between N-S Digital TV and Super TV.*** Super TV granted N-S Digital TV the exclusive right to sell its software products relating to advertisement editing and CA systems and other software products as agreed by the parties. The amount, price and related fees will be specified by each order provided by N-S Digital TV to Super TV. The agreement has a term of five years and is terminable by Super TV at any time. In 2011, Digital Rights Management, a content protection system for IPTV, was sold under the framework agreement. The aggregate value of transactions between N-S Digital TV and Super TV under this agreement was RMB2.1 million (US\$0.3 million) in 2012.

**Shareholder Rights and Corporate Governance*****Equity Transfer Option Agreement***

An equity transfer option agreement was entered into among Super TV, N-T Information Engineering and Li Yang on June 7, 2004, as amended by a supplemental agreement, dated September 1, 2005, among Super TV, N-T Information Engineering, Li Yang and N-S Digital TV, and further amended by a second supplemental agreement, dated August 18, 2007, among Super TV, N-T Information Engineering, Li Yang, N-S Digital TV and Wei Gao, a third supplemental agreement, dated June 20, 2008, among Super TV, N-S Digital TV, N-T Information Engineering, Wei Gao and Junming Wu, a fourth supplemental agreement, dated November 24, 2008, among Super TV, N-S Digital TV, N-T Information Engineering, Junming Wu, Lei Zhang and Shizhou Shen, a fifth supplemental agreement, dated July 11, 2011, among Super TV, N-S Digital TV, Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang, and a supplemental agreement, dated February 9, 2012, among Super TV, N-S Digital TV, Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen, referred to collectively as the Equity Transfer Option Agreement. Pursuant to the Equity Transfer Option Agreement, Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen, being all the shareholders of N-S Digital TV, jointly grant Super TV an exclusive and irrevocable option to purchase all of their equity interests in N-S Digital TV at any time that Super TV deems fit. Super TV may purchase such equity interests by itself or designate another party to purchase such equity interests. The total consideration for the granting of the option was RMB10 (US\$1.5). The exercise price of the option will be determined by Super TV or its designated third party at the time of the exercise, subject to the requirements of the PRC law or approval of relevant authorities with respect to the minimum purchase price and the basis for the determination of the purchase price. Following any exercise of the option, the parties will enter into a definitive equity interest transfer agreement within two days, or any period agreed to among the parties, after a written notice of exercise is delivered. The Equity Transfer Option Agreement does not have a specified term and will remain in effect unless terminated with the written consent of Super TV.

Pursuant to the Equity Transfer Option Agreement, at all times before Super TV acquires 100% of the equity interests in N-S Digital TV, without Super TV's consent, N-S Digital TV may not (i) amend its organizational documents, increase or reduce its registered capital or otherwise change its capital structure; (ii) sell, transfer, pledge or otherwise dispose of any legal or beneficial interest in any of its assets, business or revenues, or allow the creation of any encumbrance thereon; (iii) engage in any activities that may negatively impact its operations or the value of its assets; or (iv) incur, assume or guarantee any debts except in the ordinary course of business, extend any loan or credit to any person, enter into any material contracts, or engage in any merger or combination with, acquisition of, or make investment in, any other person.

## **Table of Contents**

Under the Equity Transfer Option Agreement, Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen undertake not to do any of the following without Super TV's consent, at all times before Super TV acquires 100% of the equity interests in N-S Digital TV: (i) transfer or pledge to any third party their equity interests in N-S Digital TV; (ii) cause N-S Digital TV to issue new shares or engage in any transactions that will result in changes to their existing shareholding structures or transfer to any third party N-S Digital TV's equity interests in their respective associated companies; (iii) receive any dividends, loan interest or other benefits from N-S Digital TV; or (iv) make any material adjustment or change to N-S Digital TV's business and operations.

### ***Business Operating Agreement***

A business operating agreement, dated September 1, 2005, was entered into among Super TV, N-T Information Engineering, Li Yang and N-S Digital TV, as amended by a supplemental agreement, dated August 18, 2007, among Super TV, N-S Information Engineering, Li Yang, N-S Digital TV and Wei Gao, and further amended by a second supplemental agreement, dated June 20, 2008, among Super TV, N-S Digital TV, N-T Information Engineering, Wei Gao and Junming Wu, a third supplemental agreement, dated November 24, 2008, among Super TV, N-S Digital TV, N-T Information Engineering, Junming Wu, Lei Zhang and Shizhou Shen, a fourth supplemental agreement, dated July 11, 2011, among Super TV, N-S Digital TV, Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang, and a supplemental agreement, dated February 9, 2012, among Super TV, N-S Digital TV, Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen, referred to collectively as the Business Operating Agreement. Pursuant to the Business Operating Agreement, N-S Digital TV and its shareholders agreed to (i) accept the policies and guidelines furnished by Super TV from time to time with respect to the hiring and dismissal of employees, operational management and financial system of N-S Digital TV; (ii) appoint the candidates recommended by Super TV as directors of N-S Digital TV and appoint the senior management personnel of Super TV as the general manager, chief financial officer and other senior officers of N-S Digital TV based on Super TV's recommendations; (iii) replace or remove any director or senior management personnel of N-S Digital TV at Super TV's request; and (iv) seek a guarantee from Super TV first when any guarantee is required to secure performance by N-S Digital TV of any contract or working capital loans borrowed by N-S Digital TV and pledge its assets and receivables to Super TV as a counter-guarantee. To date, N-S Digital TV has not sought any such guarantee from Super TV. In addition, Super TV has agreed with N-S Digital TV to serve as a guarantor of N-S Digital TV with respect to contracts or transactions entered into between N-S Digital TV and third parties in respect of N-S Digital TV's business operations. However, as of the date of this annual report, N-S Digital TV has not asked Super TV to provide, and Super TV has not provided, any such guarantee in favor of a third party. The Business Operating Agreement has a term of ten years and may be renewed at the option of Super TV by giving written notice for a term to be determined by Super TV. Super TV may terminate this agreement at any time by giving 30 days' advance written notice to the other parties to this agreement.

### ***Powers of Attorney***

Each of Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen executed an irrevocable power of attorney, dated January 16, 2012, to appoint Super TV or a third party designated by Super TV as an attorney-in-fact to exercise all his voting rights as a shareholder of N-S Digital TV. The term of the powers of attorney is ten years, subject to earlier termination in the event of the termination of the relevant share pledge agreement. The powers of attorney will be automatically renewed upon the extension of the term of the relevant share pledge agreement.

### ***Share Pledge Agreements***

N-T Information Engineering and Super TV entered into a share pledge agreement, dated September 1, 2005, pursuant to which N-T Information Engineering had pledged all of its equity interests in N-S Digital TV to Super TV to secure the payment obligations of N-S Digital TV under certain contractual arrangements between N-S Digital TV and Super TV. This agreement was terminated on November 24, 2008, following the transfer by N-T Information Engineering of all of its equity interests in N-S Digital TV to Lei Zhang and Shizhou Shen. On November 24, 2008, Mr. Zhang and Mr. Shen each entered into a share pledge agreement with Super TV, pursuant to which Mr. Zhang and Mr. Shen have pledged all of their respective equity interests in N-S Digital TV to Super TV to secure their respective payment obligations under their respective loan agreements with Super TV, each dated November 24, 2008.

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**Table of Contents**

Pursuant to the share pledge agreement, dated September 1, 2005, between Super TV and Li Yang, as amended by a supplemental agreement, dated August 18, 2007, between Super TV, Li Yang and Wei Gao, and further amended by a second supplemental agreement, dated June 20, 2008, among Super TV, Wei Gao and Junming Wu, Mr. Wu has pledged all of his equity interests in N-S Digital TV to Super TV to secure the payment obligations of N-S Digital TV under certain contractual arrangements between N-S Digital TV and Super TV. This agreement was terminated on July 11, 2011, following the transfer by Mr. Wu of all of his equity interests in N-S Digital TV to Tianxing Wang.

Each of Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen entered into a share pledge agreement with Super TV on July 11, 2011, which was superseded by another share pledge agreement with Super TV on January 16, 2012. Pursuant to the share pledge agreements, each of Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen has pledged all his equity interests in N-S Digital TV to Super TV to secure his and N-S Digital TV's performance of their respective obligations under the VIE contractual arrangements between N-S Digital TV or its shareholders and Super TV. Under such share pledge agreements, each of Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen has agreed not to transfer his equity interests in N-S Digital TV or create, or allow the creation of, any pledge on their respective equity interests in N-S Digital TV that may affect Super TV's interests without Super TV's consent. Pursuant to such agreements, Super TV is entitled to receive the dividends on the pledged equity interests during the term of the pledge. The duration of each of the share pledge agreements is equivalent to the maximum duration of the VIE contractual arrangements between N-S Digital TV and/or its shareholders and Super TV. The share pledge agreements may only be terminated: (i) by Super TV in writing; or (ii) upon the fulfillment of N-S Digital TV's and its shareholders' respective obligations under the VIE contractual arrangements between N-S Digital TV and/or its shareholders and Super TV, which is subject to Super TV's written confirmation. The share pledge agreements were registered with the Beijing Administration of Industry and Commerce on February 1, 2012.

***Loan Agreements***

Pursuant to two loan agreements, each dated November 24, 2008, between Super TV and each of Lei Zhang and Shizhou Shen, respectively, as amended by a supplemental agreement to the loan agreements, dated January 16, 2012, among Super TV, Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen, Super TV provided a loan in the principal amount of RMB6.2 million (US\$0.9 million) to each of Mr. Zhang and Mr. Shen. The term of each loan is ten years, which is automatically renewable for another ten years upon its termination date, unless a written notice has been provided by Super TV one month prior to such termination date. Mr. Zhang and Mr. Shen may not repay the loan prior to the termination date of the relevant loan agreement, unless so requested by Super TV, and may only repay the loan by (i) transferring all his equity interests in N-S Digital TV to Super TV or any third party designated by Super TV and (ii) paying Super TV with the entire proceeds obtained by himself from such transfer. The interest rate of each loan is nil. Super TV provided such loans to Mr. Zhang and Mr. Shen to fund their acquisitions of N-T Information Engineering's equity interests in N-S Digital TV.

Pursuant to three loan agreements, each dated July 11, 2011, between Super TV and each of Wenjun Wang, Tianxing Wang and Lei Zhang, respectively, as amended by a supplemental agreement to the loan agreements, dated January 16, 2012, among Super TV, Wenjun Wang, Tianxing Wang, Lei Zhang and Shizhou Shen, and as further amended by a second supplemental agreement, dated April 12, 2013, between Super TV and Tianxing Wang, Super TV provided a loan in the principal amount of RMB43.3 million (US\$6.7 million), RMB38.6 million (US\$6.0 million) and RMB35.1 million (US\$5.5 million) to each of Wenjun Wang, Tianxing Wang and Lei Zhang. The term of each loan is ten years, which is automatically renewable for another ten years upon its termination date, unless a written notice has been provided by Super TV one month prior to such termination date. Wenjun Wang, Tianxing Wang and Lei Zhang may not repay the loan prior to the termination date of the relevant loan agreement, unless so requested by Super TV, and may only repay the loan by (i) transferring all his equity interests in N-S Digital TV to Super TV or any third party designated by Super TV and (ii) paying Super TV with the entire proceeds obtained by himself from such transfer. The interest rate of each loan is nil. Super TV provided such loans to Wenjun Wang, Tianxing Wang and Lei Zhang in July 2011 to fund their additional contribution to N-S Digital TV's registered capital.

## **Table of Contents**

### **Other Related Party Transactions**

#### ***Shareholders Agreement***

Pursuant to the First Amended and Restated Shareholders Agreement of China Digital TV Holding Co., Ltd., or the Shareholders Agreement, dated September 13, 2007, among N-T Information Engineering, N-S Digital TV, CDTV BVI, China Capital, China Cast, SAIF, Capital Funds and certain other shareholders, as amended by an agreement, dated June 14, 2011, among us, N-S Digital TV, China Cast, SAIF, Capital Funds and certain other shareholders, at any time beginning six months after the closing of our initial public offering, each of SAIF, Capital Funds and China Capital may, on three occasions only, require us to effect the registration on a form other than Form F-3 of all or part of the registrable securities then outstanding. In addition, any holder of registrable securities may require us to effect a registration statement on Form F-3 (or any successor form or any comparable form for a registration in a jurisdiction other than the United States) for a public offering of registrable securities so long as we are entitled to use Form F-3 (or a comparable form) for such offering. Demand for a registration on Form F-3 may be made on unlimited occasions, although we are not obligated to effect more than one such registration per shareholder in any six-month period.

Registrable securities are ordinary shares not previously sold to the public and issued or issuable or sold to SAIF, Capital Funds and China Capital, including: (a) ordinary shares issuable upon conversion or exercise of either (i) any of the Series A preferred shares, or (ii) any options or warrants to purchase ordinary shares or the Series A preferred shares of our company; (b) ordinary shares held by Capital Funds and China Capital; (c) ordinary shares issued pursuant to share splits, share dividends, and similar distributions to SAIF, Capital Funds and China Capital; and (d) any other securities of our company granted with registration rights pursuant to the Shareholders Agreement.

Holders of registrable securities also have piggyback registration rights, which may require us to register all or any part of the registrable securities then held by such holders when we register any of our ordinary shares.

We are generally required to bear all of the registration expenses incurred in connection with three demand registrations on a form other than Form F-3 for each of SAIF, Capital Funds and China Capital, unlimited Form F-3 and piggyback registrations, except underwriting discounts and selling commissions, but including reasonable expenses of one counsel for the party exercising the registration right. The registration rights under the Shareholders Agreement shall terminate on June 14, 2015.

#### ***Interest Payment Agreement***

Pursuant to an agreement, dated November 30, 2006, between Super TV and N-S Digital TV, N-S Digital TV agreed to pay interest at a rate equal to commercial banks lending rate for one-year loans on the payments payable by N-S Digital TV to Super TV for the purchases of products from Super TV. Interest payable will start to accrue from the first day of the month following the confirmation of the corresponding sales until the actual payment. No interest was accrued as of December 31, 2012 under this agreement.

### **C. Interests of Experts and Counsel**

Not Applicable.

## **Item 8. Financial Information**

### **A. Consolidated Statements and Other Financial Information**

#### **Consolidated Statements**

See Item 18. Financial Statements.

## **Table of Contents**

### **Legal Proceedings**

We are not currently a party to any material legal proceeding and, to our knowledge, there are no material legal proceedings threatened against us. From time to time, we may be subject to various claims and legal actions arising in the ordinary course of business.

### **Dividend Policy**

In December 2008, in the belief that a special dividend is an efficient use of our cash to maximize shareholder value, our board of directors determined to declare and pay a special cash dividend of US\$1.00 per ordinary share of the company. This special dividend in the amount of US\$57.3 million was fully paid by the end of February 2009.

In November 2010, our board of directors declared a special cash dividend of US\$2.00 per ordinary share to be paid in two installments of US\$1.00 each. The special cash dividend was fully paid on May 31, 2011.

In May 2011, our board of directors declared a special cash dividend of US\$0.56 per ordinary share. The dividend was fully paid by April 13, 2012.

In November 2012, our board of directors declared a special cash dividend of US\$2.30 per ordinary share to be paid in two installments of US\$1.00 and US\$1.30, respectively.

Our board of directors has the discretion to determine the payment of any dividends. As a matter of company policy, our board of directors will consider declaring and paying dividends for a given period, subject to the board of directors' determination that (i) we have sufficient profit attributable to shareholders for such period and (ii) our funding requirements can be fully satisfied if a proposed dividend is declared and paid. Our board of directors will review and decide whether to revise our dividend policy, from time to time, in light of our future operations and earnings, capital requirements and surplus, financial condition, contractual restrictions, general business conditions and other factors as the board of directors may deem relevant.

We may rely on our operating subsidiary, Super TV, for our cash needs, including the funds necessary to pay dividends to our shareholders. The payment of dividends by Super TV is subject to limitations. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China We may rely on dividends and other distributions on equity paid by our operating subsidiary to fund cash and financing requirements, and limitations on the ability of our operating subsidiary to pay dividends to us could materially restrict on our ability to conduct our business.

Holders of ADSs will be entitled to receive dividends, subject to the terms of the deposit agreement, less the fees and expenses payable under the deposit agreement. Cash dividends will be paid by the depositary to holders of ADSs in U.S. dollars. Other distributions, if any, will be paid by the depositary to holders of our ADSs in any means it deems legal, fair and practical.

### **B. Significant Changes**

There have been no significant changes since December 31, 2012, the date of the annual financial statements in this annual report.

## **Item 9. The Offer and Listing**

### **A. Offering and Listing Details**

#### **Market and Share Price Information**

Our ADSs, each representing one ordinary share, have been listed on the NYSE since October 5, 2007. Our ADSs trade under the symbol STV. The NYSE is the principal trading market for our ADSs, which are not listed on any other exchanges in or outside the United States.

**Table of Contents**

The high and low closing prices of our ADSs on the NYSE since listing are as follows:

|                               | Price per ADS (US\$) |      |
|-------------------------------|----------------------|------|
|                               | High                 | Low  |
| <b>Yearly:</b>                |                      |      |
| 2008                          | 27.55                | 4.25 |
| 2009                          | 11.31                | 5.83 |
| 2010                          | 9.21                 | 5.30 |
| 2011                          | 7.42                 | 3.17 |
| 2012                          | 4.35                 | 1.68 |
| <b>Quarterly:</b>             |                      |      |
| First Quarter, 2011           | 7.42                 | 5.82 |
| Second Quarter, 2011          | 7.34                 | 5.02 |
| Third Quarter, 2011           | 5.44                 | 3.88 |
| Fourth Quarter, 2011          | 4.24                 | 3.17 |
| First Quarter, 2012           | 4.05                 | 3.27 |
| Second Quarter, 2012          | 3.71                 | 2.56 |
| Third Quarter, 2012           | 3.18                 | 2.60 |
| Fourth Quarter, 2012          | 4.35                 | 1.68 |
| First Quarter, 2013           | 2.27                 | 1.70 |
| <b>Monthly:</b>               |                      |      |
| October 2012                  | 2.97                 | 2.79 |
| November 2012                 | 4.35                 | 2.05 |
| December 2012                 | 2.08                 | 1.68 |
| January 2013                  | 1.90                 | 1.70 |
| February 2013                 | 2.27                 | 1.87 |
| March 2013                    | 1.96                 | 1.73 |
| April 2013 (through April 15) | 1.81                 | 1.74 |

As of March 31, 2013, a total of 30,675,560 ADSs were outstanding, excluding the 421,526 ADSs that were held for our account in preparation for exercise of share options by option holders under our employee stock incentive plans. As of March 31, 2013, 30,675,560 ordinary shares were registered in the name of Deutsche Bank Trust Company Americas, the depository under the deposit agreement, excluding 421,526 ordinary shares that were issued and held for our account in preparation for exercise of share options by option holders under our employee stock incentive plans.

**B. Plan of Distribution**

Not Applicable.

**C. Markets**

Our ADSs, each representing one ordinary share, have been listed on the NYSE since October 5, 2007 under the symbol STV.

**D. Selling Shareholders**

Not Applicable.

**E. Dilution**

Not Applicable.

**F. Expenses of the Issue**

Not Applicable.



## **Table of Contents**

### **Item 10. Additional Information**

#### **A. Share Capital**

Not Applicable.

#### **B. Memorandum and Articles of Association**

We incorporate by reference into this annual report the description of our Second Amended and Restated Memorandum and Articles of Association contained in our registration statement on Form F-1 (File No. 333-146072) filed with the SEC on September 14, 2007. Our shareholders adopted our Second Amended and Restated Memorandum and Articles of Association on September 13, 2007.

#### **C. Material Contracts**

Other than the contracts described elsewhere in this annual report, we and our operating companies have not entered into any material contracts that are not in the ordinary course of business within the two years preceding the date of this annual report.

#### **D. Exchange Controls**

The Cayman Islands currently have no exchange control restrictions. Also see Item 4. Information on the Company B. Business Overview Regulation Foreign Currency Exchange and Regulation of Foreign Exchange in Certain Onshore and Offshore Transactions for information on foreign currency exchange in the PRC.

#### **E. Taxation**

The following discussion of the material Cayman Islands and United States federal income tax consequences of an investment in the ADSs is based upon laws and relevant interpretations thereof in effect as of the date of this annual report, all of which are subject to change. This summary does not deal with all possible tax consequences relating to an investment in the ADSs, such as the tax consequences under state, local and other tax laws.

#### **Cayman Islands Taxation**

To the extent the following discussion relates to Cayman Islands law with respect to the income tax consequence of an investment in our ADSs, it represents the opinion of Conyers Dill & Pearman (Cayman) Limited.

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciations and there is no taxation in the nature of inheritance tax or estate duty or withholding tax applicable to us or to any holder of ADSs or ordinary shares. There are no other taxes likely to be material to us levied by the Government of the Cayman Islands except for stamp duties which may be applicable on instruments executed in, or after execution brought within the jurisdiction of, the Cayman Islands. No stamp duty is payable in the Cayman Islands on transfers of shares of Cayman Islands companies except those which hold interests in land in the Cayman Islands. The Cayman Islands is not party to any double tax treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.

Pursuant to Section 6 of the Tax Concessions Law (1999 Revision) of the Cayman Islands, we have obtained an undertaking from the Governor-in-Cabinet:

that no law which is enacted in the Cayman Islands imposing any tax to be levied on profits or income or gains or appreciations shall apply to the Company or its operations; and

that the aforesaid tax or any tax in the nature of estate duty or inheritance tax shall not be payable on the shares, debentures or other obligations of the Company.



## **Table of Contents**

The undertaking for us is for a period of 20 years from May 1, 2007.

### **United States Federal Income Taxation**

This section describes the material United States federal income tax consequences of owning ADSs. It applies to you only if you are a U.S. holder as defined below, and you hold your ADSs as capital assets for tax purposes. This section does not apply to you if you are a member of a special class of holders subject to special rules, including:

a dealer in securities,

a trader in securities that elects to use a mark-to-market method of accounting for securities holdings,

a tax-exempt organization,

a life insurance company,

a person liable for alternative minimum tax,

a person that actually or constructively owns 10% or more of our voting stock,

a person that holds ADSs as part of a straddle or a hedging or conversion transaction,

a person that purchases or sells ADSs as part of a wash sale for tax purposes, or

a person whose functional currency is not the U.S. dollar.

**U.S. holders are urged to consult their tax advisors about the application of the United States federal tax rules to their particular circumstances as well as the state, local and foreign tax consequences to them of the purchase, ownership and disposition of our ADSs or ordinary shares.**

This section is based on the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed Treasury regulations, published rulings and court decisions, all as currently in effect. These laws are subject to change, possibly on a retroactive basis. In addition, this section is based in part upon the representations of the depositary and the assumption that each obligation in the Deposit Agreement and any related agreement will be performed in accordance with its terms.

If a partnership holds the ADSs, the United States federal income tax treatment of a partner will generally depend on the status of the partner and the tax treatment of the partnership. A partner in a partnership holding the ADSs should consult its tax advisor with respect to the United States federal income tax treatment of an investment in the ADSs.

You are a U.S. holder if you are a beneficial owner of ADSs and you are:

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a citizen or resident of the United States,

a corporation (or other entity taxable as a corporation for United States federal income tax purposes) organized under the laws of the United States, any State or the District of Columbia,

an estate whose income is subject to United States federal income tax regardless of its source, or

a trust if a United States court can exercise primary supervision over the trust's administration and one or more United States persons are authorized to control all substantial decisions of the trust.

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## **Table of Contents**

In general, and taking into account the earlier assumptions, for United States federal income tax purposes, if you hold ADRs evidencing ADSs, you will be treated as the owner of the shares represented by those ADRs. Exchanges of shares for ADRs, and ADRs for shares, generally will not be subject to United States federal income tax. The tax treatment of holding shares is identical to that of holding ADSs.

### ***Taxation of Dividends***

Under the United States federal income tax laws, and subject to PFIC rules discussed below, the gross amount of any dividend we pay out of our current or accumulated earnings and profits (as determined for United States federal income tax purposes) is subject to United States federal income taxation. If you are a non-corporate U.S. holder, including an individual, dividends that constitute qualified dividend income will be taxable to you at the preferential rates applicable to long-term capital gains provided that you hold the ADSs for more than 60 days during the 121-day period beginning 60 days before the ex-dividend date and meet other holding period requirements. Dividends we pay with respect to the ADSs generally will be qualified dividend income provided that, in the year that you receive the dividend, the ADSs are readily tradable on an established securities market in the United States. The NYSE should qualify as an established securities market in the United States.

You must include any foreign tax withheld from the dividend payment in this gross amount even though you do not in fact receive it. The dividend is taxable to you when the depository receives the dividend, actually or constructively. The dividend will not be eligible for the dividends-received deduction generally allowed to United States corporations in respect of dividends received from other United States corporations. Distributions in excess of current and accumulated earnings and profits, as determined for United States federal income tax purposes, will be treated as a non-taxable return of capital to the extent of your basis in the ADSs and thereafter as capital gain.

Subject to certain limitations, in the event that PRC tax is withheld and paid over to the PRC with regard to the dividend payments, the PRC tax will generally be creditable or deductible against your United States federal income tax liability. See Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China Dividends payable by us to our non-PRC shareholders and ADS holders, and gains on the sales of our ordinary shares or ADSs, may be subject to withholding taxes under PRC tax laws, which may materially reduce the value of your investment. Special rules apply in determining the foreign tax credit limitation with respect to dividends that are subject to the preferential tax rates. To the extent a refund of the tax withheld is available under PRC law, the amount of tax withheld that is refundable will not be creditable against your United States federal income tax liability.

Dividends will generally be income from sources outside the United States, and, depending on your circumstances, will be either passive or general category income for purposes of computing the foreign tax credit allowable to you.

### ***Taxation of Capital Gains***

Subject to the PFIC rules discussed below, if you sell or otherwise dispose of your ADSs, you will recognize capital gain or loss for United States federal income tax purposes equal to the difference between the U.S. dollar value of the amount that you realize and your tax basis, determined in U.S. dollars, in your ADSs. Capital gain of a non-corporate U.S. holder, including an individual, is generally taxed at preferential rates where the holder has a holding period greater than one year. The gain or loss will generally be income or loss from sources within the United States for foreign tax credit limitation purposes.

### ***PFIC Rules***

Based on an analysis of the value of our assets as of December 31 for the years 2009 through 2012, we were a PFIC during the taxable years 2009 through 2012 for U.S. federal income tax purposes. This conclusion is a factual determination that is made annually and thus we may or may not be a PFIC for the taxable year of 2013 and thereafter.

In general, we will be a PFIC with respect to you if for any taxable year in which you held our ADSs:

at least 75% of our gross income for the taxable year is passive income, or

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## **Table of Contents**

at least 50% of the value, determined on the basis of a quarterly average, of our assets is attributable to assets that produce or are held for the production of passive income.

Passive income generally includes dividends, interest, royalties, rents (other than certain rents and royalties derived in the active conduct of a trade or business), annuities and gains from assets that produce passive income. If a foreign corporation owns at least 25% by value of the stock of another corporation, the foreign corporation is treated for purposes of the PFIC tests as owning its proportionate share of the assets of the other corporation, and as receiving directly its proportionate share of the other corporation's income.

Because we were classified as a PFIC for the years described above, you will generally be subject to the special PFIC tax rules or, if you make a mark-to-market election, the mark-to-market rules as described below.

**Special PFIC Rules.** If we are treated as a PFIC, and you are a U.S. holder that did not make a mark-to-market election, you will be subject to special rules with respect to:

any gain you realize on the sale or other disposition of your ADSs, and

any excess distribution that we make to you (generally, any distributions to you during a single taxable year that are greater than 125% of the average annual distributions received by you in respect of the ADSs during the three preceding taxable years or, if shorter, your holding period for the ADSs).

Under these rules:

the gain or excess distribution will be allocated ratably over your holding period for the ADSs,

the amount allocated to the taxable year in which you realized the gain or excess distribution will be taxed as ordinary income,

the amount allocated to each prior year, with certain exceptions, will be taxed at the highest tax rate in effect for that year, and

the interest charge generally applicable to underpayments of tax will be imposed in respect of the tax attributable to each such year. Special rules apply for calculating the amount of the foreign tax credit with respect to excess distributions by a PFIC.

Moreover, your ADSs will be treated as stock in a PFIC if we were a PFIC at any time during your holding period in your ADSs, even if we are not currently a PFIC. For purposes of this rule, if you make a mark-to-market election with respect to your ADSs, you will be treated as having a new holding period in your ADSs beginning on the first day of the first taxable year beginning after the last taxable year for which the mark-to-market election applies. In addition, notwithstanding any election you make with regard to the ADSs, dividends that you receive from us will not constitute qualified dividend income to you if we are a PFIC either in the taxable year of the distribution or the preceding taxable year. Dividends that you receive that do not constitute qualified dividend income are not eligible for taxation at the preferential rates applicable to qualified dividend income. Instead, you must include the gross amount of any such dividend paid by us out of our accumulated earnings and profits (as determined for United States federal income tax purposes) in your gross income, and it will be subject to tax at rates applicable to ordinary income.

**Mark-to-Market Rules.** If you own ADSs in a PFIC that are treated as marketable stock, you should generally be able to make a mark-to-market election. We believe that our ADSs are and will continue to be marketable stock as long as they continue to be traded on NYSE, other than in *de minimis* quantities, on at least 15 days during each calendar quarter. If you make this election, you will not be subject to the PFIC rules described above. Instead, in general, you will include as ordinary income each year the excess, if any, of the fair market value of your ADSs at the end of the taxable year over your adjusted basis in your ADSs. These amounts of ordinary income will not be eligible for the favorable tax rates applicable to qualified dividend income or long-term capital gains. You will also be allowed to take an ordinary loss in respect of the excess, if any, of the adjusted basis of your ADSs over their fair market value at the end of the taxable year (but only to the extent

of the net amount of previously included income as a result of the mark-to-market election). Your basis in the ADSs will be adjusted to reflect any such income or loss amounts.

## **Table of Contents**

If you own ADSs during any year that we are a PFIC with respect to you, you must file Internal Revenue Service Form 8621.

### **F. Dividends and Paying Agents**

Not Applicable.

### **G. Statement by Experts**

Not Applicable.

### **H. Documents on Display**

You can read and copy documents referred to in this annual report that have been filed with the SEC at the SEC's public reference room located at 100 F Street, NE, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms and their copy charges. The SEC also maintains a website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system.

### **I. Subsidiary Information**

Not Applicable.

## **Item 11. Quantitative and Qualitative Disclosures About Market Risks**

### **Interest Rate Risk**

As of December 31, 2012, we had no short-term or long-term borrowings. Our exposure to market risk for changes in interest rates relates primarily to the interest income generated by our cash deposits with the banks. We have not used any derivative financial instruments in our investment portfolio. Interest earning instruments carry a degree of interest rate risk. We have not been exposed, nor do we anticipate being exposed to material risks due to changes in interest rates. However, our future interest income may fall short of expectations due to changes in interest rates. In addition, we may borrow loans in the future and changes in interest rates may affect our finance cost.

### **Foreign Currency Risk**

Although the conversion of the Renminbi is highly regulated in the PRC, the value of the Renminbi against the value of the U.S. dollar (or any other currency) nonetheless may fluctuate and be affected by, among other things, changes in the political and economic conditions in the PRC. Under the currency policy in effect in the PRC today, the Renminbi is permitted to fluctuate in value within a narrow band against a basket of certain foreign currencies. The PRC is currently under significant international pressures to liberalize this government currency policy, and if such liberalization were to occur, the value of the Renminbi could appreciate or depreciate against the U.S. dollar.

Fluctuations in exchange rates may affect our costs, profit margins and net income. For example, in 2012, substantially all of our revenues were denominated in Renminbi and approximately 29.5% of our cost of revenues was denominated in U.S. dollars. In 2012, fluctuations in the exchange rates between the Renminbi and U.S. dollar and other foreign currencies resulted in an increase in our net income of approximately US\$0.03 million.

## **Table of Contents**

Fluctuations in exchange rates may also affect our balance sheet. For example, to the extent that we need to convert U.S. dollars received in our initial public offering into the Renminbi for our operations, appreciation of the Renminbi against the U.S. dollar would have an adverse effect on the Renminbi amount that we receive from the conversion. Conversely, if we decide to convert our Renminbi into U.S. dollars for the purpose of making payments for dividends on our ordinary shares or ADSs or for other business purposes, appreciation of the U.S. dollar against the Renminbi would have a negative effect on the U.S. dollar amount available to us. Considering the amount of our cash and cash equivalents as of December 31, 2012, a 1.0% appreciation of the Renminbi against the U.S. dollar will result in an estimated increase of approximately US\$1.2 million in our total amount of cash and cash equivalents, and a 1.0% appreciation of the U.S. dollar against the Renminbi will result in a decrease of approximately US\$1.2 million in our total cash and cash equivalents.

Also see Item 3. Key Information D. Risk Factors Risks Relating to the People's Republic of China Fluctuations in exchange rates could result in foreign exchange currency losses.

In April and May 2011, we entered into foreign currency forward contracts to facilitate the payment of a special cash dividend declared in November 2010, in an effort to reduce our exposure to foreign currency exchange risk. These foreign currency forward contracts expired in the second quarter of 2012.

### **Inflation**

In recent years, inflation has not had a material impact on our results of operations. According to the National Bureau of Statistics of China, the change in Consumer Price Index in the PRC was 3.3%, 5.4% and 2.6% in 2010, 2011 and 2012, respectively. Although we have not been materially affected by inflation since our inception, we cannot assure you that we will not be affected in the future by higher rates of inflation in the PRC.

## **Item 12. Description of Securities Other than Equity Securities**

### **A. Debt Securities.**

Not Applicable.

### **B. Warrants and Rights.**

Not Applicable.

### **C. Other Securities.**

Not Applicable.

### **D. American Depositary Shares.**

#### **Fees and Charges for Holders of American Depositary Receipts**

Our American Depositary Receipt, or ADR, facility is maintained by Deutsche Bank Trust Company Americas, or DBTCA, pursuant to a deposit agreement dated as of October 11, 2007, or the Deposit Agreement, by and among us, DBTCA, and holder and beneficial owners of ADSs evidenced by ADRs issued thereunder. We use the term "holder" in this discussion to refer to the person in whose name an ADR is registered.

In accordance with the terms of the Deposit Agreement, DBTCA may charge holders of our ADSs, either directly or indirectly, fees or charges up to the amounts described below.

US\$5.00 for each 100 ADSs, or any portion thereof, issued or surrendered, for:

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each issuance of ADSs, including upon the deposit of shares or to any person to whom an ADS distribution is made pursuant to share dividends or other free distributions of shares, bonus distributions, share splits or other distributions (except where converted to cash); and

**Table of Contents**

each surrender of ADSs for cancellation and withdrawal of deposited securities, including cash distributions made pursuant to a cancellation or withdrawal;

US\$2.00 per 100 ADSs for distribution of cash proceeds pursuant to a cash distribution (so long as the charging of such fee is not prohibited by any exchange upon which the ADSs are listed), sale of rights and other entitlements, not made pursuant to a cancellation or withdrawal;

US\$5.00 per 100 ADSs, or any portion thereof, issued upon the exercise of rights;

an annual fee of US\$0.02 per ADS for the operation and maintenance costs in administering the facility; and

in connection with inspections of the relevant share register maintained by the local registrar, if applicable undertaken by DBTCA, its custodian or their respective agents: an annual fee of US\$0.01 per ADS (such fee to be assessed against holders of record as of the date or dates set by DBTCA as it sees fit and collected at the sole discretion of DBTCA by billing such holders for such fee or by deducting such fee from one or more cash dividends or other cash distributions).

In addition, holders or beneficial owners of our ADSs, persons depositing shares for deposit and persons surrendering ADSs for cancellation and withdrawal of deposited securities may be required to pay DBTCA the following charges:

taxes, including applicable interest and penalties, and other governmental charges;

transfer or registration fees for the registration of transfer of deposited securities on any applicable register in connection with the deposit or withdrawal of deposited securities, including those of a central depository for securities (where applicable);

certain cable, telex, facsimile and electronic transmission and delivery expenses;

expenses incurred by DBTCA in connection with the conversion of foreign currency into U.S. dollars;

fees and expenses incurred by DBTCA in connection with compliance with exchange control regulations and other regulatory requirements applicable to the shares, deposited securities and ADSs; and

any additional fees, charges, costs or expenses that may be incurred by DBTCA from time to time.

The fees charged upon issuance of ADSs are imposed on the person to whom ADSs are issued, and in the case of withdrawals and cancellations, on the person surrendering the ADSs. In the case of cash distributions, service fees are generally deducted from the cash being distributed. In the case of distributions other than cash, such as stock dividends and rights, the depository charges the applicable ADS record date holder concurrent with the distribution. Annual fees may be collected from holders of ADSs in a manner determined by DBTCA. In the case of ADSs registered in the name of the investor (whether certificated or in book-entry form), DBTCA sends invoices to holders of our ADSs as of the applicable record date. In the case of ADSs being held in brokerage and custodian accounts (via The Depository Trust and Clearing Corporation, or DTCC), DBTCA may, if permitted by the settlement systems provided by DTCC, collect the fees through such settlement systems (whose nominee is the registered holder of the ADSs held in DTCC) from the brokers and custodians holding the ADSs in their DTCC accounts. The brokers and custodians who hold their clients' ADSs in DTCC accounts in such case may in turn charge their clients' accounts the amount of the service fees paid to DBTCA.

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The ADS holders are responsible for any taxes or other governmental charges payable on their ADSs or on the deposited securities underlying their ADSs. The custodian of DBTCA may refuse to deposit shares and DBTCA may refuse to issue ADSs, deliver ADRs, register the transfer, split up or combination of ADRs, or allow the relevant ADS holder to withdraw the deposited securities underlying the ADSs until such taxes or other charges, including any applicable interest and penalty, are paid. DBTCA may apply payments owed to the relevant ADS holder or sell deposited securities underlying the ADSs to pay any taxes, including interest and penalty owed, and the relevant ADS holder will remain liable for any deficiency. If DBTCA sells deposited securities, it will, if appropriate, reduce the number of ADSs to reflect the sale and pay to the relevant ADS holder any proceeds, or send to the relevant ADS holder any property remaining after it has paid the taxes.

## **Table of Contents**

### **Payment Made by DBTCA to Our Company**

For the year ended December 31, 2012, DBTCA reimbursed us US\$0.6 million for contributions towards our investor relations activities and other miscellaneous expenses related to the listing of our ADSs on the NYSE. In addition, DBTCA paid an aggregate of US\$25,961 on our behalf for organizing our annual general shareholders' meeting for the year of 2012.

## **PART II**

### **Item 13. Defaults, Dividend Arrearages and Delinquencies**

None.

### **Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds** **Material Modifications to the Rights of Security Holders**

See Item 10. Additional Information for a description of the rights of securities holders, which remain unchanged.

#### **Use of Proceeds**

The net proceeds to us from our initial public offering in connection with which we filed our registration statement on Form F-1 (File No. 333-146072), after deduction of fees and expenses, were approximately US\$202.2 million. We have used all of the net proceeds from our initial public offering.

### **Item 15. Controls and Procedures** **Disclosure Controls and Procedures**

Our management, with the participation of our chief executive officer and chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this annual report. Based on this evaluation, our chief executive officer and chief financial officer have concluded that, as of the end of the fiscal year covered by this annual report, our disclosure controls and procedures were designed, and were effective, to give reasonable assurance that the information required to be disclosed by us in reports that we file under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and were also effective to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our chief executive officer and chief financial officer, to allow timely decisions regarding required disclosure.

### **Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, for our company. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements in accordance with generally accepted accounting principles, and includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of a company's assets, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that a company's receipts and expenditures are being made only in accordance with authorizations of a company's management and directors, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of a company's assets that could have a material effect on the consolidated financial statements.



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## **Table of Contents**

Due to its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation, and may not prevent or detect misstatements. In addition, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

As required by Section 404 of the Sarbanes-Oxley Act and related rules as promulgated by the SEC, our management, with the participation of our chief executive officer and chief financial officer, assessed the effectiveness of the internal control over financial reporting as of December 31, 2012 using criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Based on this evaluation, our management has concluded that the internal control over financial reporting was effective as of December 31, 2012 based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

The effectiveness of our internal control over financial reporting as of December 31, 2012 has been audited by Deloitte Touche Tohmatsu Certified Public Accountants LLP, an independent registered public accounting firm, as stated in their report included elsewhere in this annual report.

### **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of China Digital TV Holding Co., Ltd.

We have audited the internal control over financial reporting of China Digital TV Holding Co. Ltd. (the Company), its subsidiaries, its variable interest entity (the VIE) and the VIE's subsidiaries (collectively, the Group) as of December 31, 2012, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Group's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

## **Table of Contents**

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Group maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2012 of the Group and our report dated April 16, 2013 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the Group's adoption of the authoritative guidance on the presentation of comprehensive income.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Beijing, the People's Republic of China

April 16, 2013

### **Changes in Internal Control Over Financial Reporting**

There were no significant changes in our internal controls over financial reporting identified in connection with the evaluation required by paragraph (d) of 17 CFR 240.13a-15 or 240.15d-15 that occurred during the period covered by this annual report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **Item 16.**

#### **Item 16A. Audit Committee Financial Expert**

Our board has determined that Mr. Songzuo Xiang, who is one of our independent directors under the applicable rules of the SEC and the NYSE, is an audit committee financial expert within the meaning of the rules of the SEC. Our board appointed Mr. Songzuo Xiang as an audit committee member, effective from December 30, 2009. See Item 6. Directors, Senior Management and Employees.

#### **Item 16B. Code of Ethics**

We have adopted a Code of Business Conduct and Ethics that applies to all our directors, officers and employees, including our chief executive officer, chief financial officer and financial controller. We have filed the Code of Business Conduct and Ethics as an exhibit to our registration statement on Form F-1 (No. 333-146072) and have posted the text of such codes on our Internet website at <http://ir.chinadtv.cn>.

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## **Table of Contents**

### **Item 16C. Principal Accountant Fees and Services**

At the direction of the PRC government in accordance with the Scheme of the Localization Restructuring of Chinese-Foreign Cooperative Accounting Firms, Deloitte Touche Tohmatsu CPA Limited, our principal external auditors, has restructured to a new partnership and changed its name to Deloitte Touche Tohmatsu Certified Public Accountants LLP, effective from January 1, 2013. Deloitte Touche Tohmatsu Certified Public Accountants LLP has succeeded Deloitte Touche Tohmatsu CPA Limited for all purposes and assumed all of the obligations and rights of Deloitte Touche Tohmatsu CPA Limited with effect from January 1, 2013. Deloitte Touche Tohmatsu CPA Limited and Deloitte Touche Tohmatsu Certified Public Accountants LLP are hereinafter referred to as "Deloitte". Deloitte has served as our independent registered public accounting firm for each of the fiscal years ended on December 31, 2011 and December 31, 2012, for which audited financial statements appear in this annual report on Form 20-F. The auditor is appointed by our board of directors and will hold office until our board of directors appoints another auditor.

#### **Audit Fees**

The aggregate fees billed in each of 2011 and 2012 for professional services rendered by our principal accountant for the audit of our annual financial statements or services that are normally provided by the accountant in connection with statutory or regulatory filings or engagements were US\$0.9 million and US\$0.9 million, respectively.

#### **Audit-Related Fees**

The aggregate fees billed in each of 2011 and 2012 for assurance and related services rendered by our principal accountant that are reasonably related to the performance of the audit or review of our financial statements and are not reported under the caption "Audit Fees" above were nil and US\$0.07 million, respectively.

#### **Tax Fees**

The aggregate fees billed in each of 2011 and 2012 for professional services relating to tax compliance, tax advice and tax planning rendered by our principal accountant were US\$0.01 million and US\$0.01 million, respectively.

#### **All Other Fees**

The aggregate fees billed in each of 2011 and 2012 for products and services provided by our principal accountant, other than the services reported above under the captions "Audit Fees", "Audit-Related Fees" and "Tax Fees", were nil and nil, respectively.

#### **Audit Committee's Pre-approval Policies and Procedures**

The audit committee of our board of directors is directly responsible for the appointment, compensation, retention and oversight of the work of the independent auditors. Pursuant to the audit committee charter adopted by the board of directors on September 13, 2007, the committee has the authority and responsibility to appoint, retain and terminate our independent auditors (subject, if applicable, to shareholder approval), and has sole authority to approve all audit engagement fees and terms. The audit committee has the power to preapprove, or to adopt appropriate procedures to preapprove, all audit and non-audit services to be provided by the independent auditors, and to consider whether the outside auditor's provision of non-audit services to us is compatible with maintaining the independence of the outside auditors. The audit committee may, in its discretion, delegate to one or more of its members the authority to preapprove any audit or non-audit services to be performed by the independent auditors, provided that such approvals are presented to the audit committee at its next scheduled meeting.

### **Item 16D. Exemptions from the Listing Standards for Audit Committees**

Not Applicable.

### **Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers**

None.

**Item 16F. Change in Registrant's Certifying Accountant**

There has been no change in our certifying accountant during our two most recent fiscal years or any subsequent interim period.

**Table of Contents**

**Item 16G. Corporate Governance**

As our ADSs are registered with the SEC and are listed on the NYSE, we are subject to corporate governance requirements imposed by both the SEC and the NYSE.

We are incorporated in the Cayman Islands. Under Section 303A of the NYSE Listed Company Manual, NYSE-listed non-U.S. companies may, in general, follow their home country corporate governance practices in lieu of some of the NYSE corporate governance requirements. A NYSE-listed non-U.S. company is required to provide a general summary of the significant differences to its U.S. investors either on the company website or its annual report distributed to its U.S. investors.

As a general matter, we are committed to a high standard of corporate governance and endeavor to comply with most of the NYSE corporate governance practices. We believe that there are no significant differences with our corporate governance policies as compared to what the NYSE requires of domestic listed companies.

**Item 16H. Mine Safety Disclosure**

Not Applicable.

**PART III**

**Item 17. Financial Statements**

We have elected to provide financial statements and related information specified in Item 18.

**Item 18. Financial Statements**

See Index to Consolidated Financial Statements for a list of all financial statements filed as part of this annual report.

**Item 19. Exhibits**

| Number             | Description of Exhibit   |
|--------------------|--|
| 1.1 <sup>(1)</sup> | Second Amended and Restated Memorandum and Articles of Association of China Digital TV Holding Co., Ltd.   |
| 2.1 <sup>(1)</sup> | Specimen of Share Certificate.   |
| 2.2 <sup>(1)</sup> | Form of Deposit Agreement, including form of American Depositary Receipts.   |
| 2.3 <sup>(1)</sup> | First Amended and Restated Shareholders Agreement of China Digital TV Holding Co., Ltd., dated September 13, 2007, among Novel-Tongfang Information Engineering Co., Ltd., Beijing Novel-Tongfang Digital TV Technology Co., Ltd., China Digital TV Technology Co., Ltd., China Capital Investment Holdings Limited, China Cast Investment Holdings Limited, SB Asia Infrastructure Fund L.P., Capital International Private Equity Fund IV, L.P., CGPE IV, L.P. and certain other shareholders. |
| 4.1 <sup>(1)</sup> | Asset Transfer Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd.  |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.2 <sup>(1)</sup>  | Equity Transfer Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd. and related (i) Equity Entrustment Agreement, dated September 10, 2004, and (ii) Equity Purchase Entrustment Agreement, dated April 1, 2004, both between the same parties.                                       |
| 4.3 <sup>(1)</sup>  | Asset Purchase Agreement, dated June 8, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.4 <sup>(1)</sup>  | Equity Transfer Agreement, dated August 4, 2006, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and related Equity Transfer Agreement, dated March 15, 2007, among Novel-Tongfang Information Engineering Co., Ltd., Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Panasonic Corporation of China. |
| 4.5 <sup>(1)</sup>  | Asset Transfer Agreement, dated August 5, 2006, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and the Supplemental Agreement thereto, dated April 6, 2007.   |
| 4.6 <sup>(1)</sup>  | Trademark Licensing Agreement entered into in March 2007 between Beijing Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd.   |
| 4.7 <sup>(1)</sup>  | Equipment Leasing Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.8 <sup>(1)</sup>  | Technical Support and Related Service Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.9 <sup>(1)</sup>  | Technology License Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.10 <sup>(1)</sup> | Technology Development Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.11 <sup>(1)</sup> | Products and Software Purchase Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.12 <sup>(3)</sup> | Letter of Consent, dated April 30, 2009, issued by Beijing Super TV Co., Ltd. to Beijing Novel-Super Digital TV Technology Co., Ltd.   |
| 4.13 <sup>(3)</sup> | Equity Transfer Agreement, dated June 20, 2008 between Wei Gao and Junming Wu for Beijing Novel-Super Digital TV Technology Co., Ltd.  |
| 4.14 <sup>(3)</sup> | Equity Transfer Agreement, dated November 24, 2008, between Novel-Tongfang Information Engineering Co., Ltd. and Shizhou Shen for Beijing Novel-Super Digital TV Technology Co., Ltd.  |
| 4.15 <sup>(3)</sup> | Equity Transfer Agreement, dated November 24, 2008, between Novel-Tongfang Information Engineering Co., Ltd. and Lei Zhang for Beijing Novel-Super Digital TV Technology Co., Ltd.   |

**Table of Contents**

| Number              | Description of Exhibit   |
|---------------------|--|
| 4.16                | Equity Transfer Option Agreement, dated June 7, 2004, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Li Yang <sup>(1)</sup> ; the Supplemental Agreement thereto, dated September 1, 2005, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. <sup>(1)</sup> ; the No. 2 Supplemental Agreement thereto, dated August 18, 2007, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang, Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Wei Gao <sup>(1)</sup> ; the No. 3 Supplemental Agreement thereto, dated June 20, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Wei Gao and Junming Wu <sup>(3)</sup> ; the No. 4 Supplemental Agreement thereto, dated November 24, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Junming Wu, Lei Zhang and Shizhou Shen <sup>(3)</sup> ; and the No. 5 Supplemental Agreement thereto, dated July 11, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang <sup>(6)</sup> . |
| 4.17 <sup>(1)</sup> | Share Pledge Agreement, dated September 1, 2005, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.18 <sup>(3)</sup> | Termination Agreement of Share Pledge, dated November 24, 2008, between Beijing Super TV Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd.  |
| 4.19                | Share Pledge Agreement, dated September 1, 2005, between Li Yang and Beijing Super TV Co., Ltd. <sup>(1)</sup> ; the Supplemental Agreement thereto, dated August 18, 2007, among Li Yang, Beijing Super TV Co., Ltd. and Wei Gao <sup>(1)</sup> ; the No. 2 Supplemental Agreement thereto, dated June 20, 2008, among Beijing Super TV Co., Ltd., Wei Gao and Junming Wu <sup>(3)</sup> ; and the Share Pledge Termination Agreement, dated July 11, 2011 between Beijing Super TV Co., Ltd. and Junming Wu <sup>(6)</sup> .   |
| 4.20 <sup>(3)</sup> | Share Pledge Agreement, dated November 24, 2008, between Shizhou Shen and Beijing Super TV Co., Ltd.   |
| 4.21 <sup>(3)</sup> | Share Pledge Agreement, dated November 24, 2008, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.22                | Business Operating Agreement, dated September 1, 2005, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. <sup>(1)</sup> ; the Supplemental Agreement thereto, dated August 18, 2007, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang, Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Wei Gao <sup>(1)</sup> ; the No. 2 Supplemental Agreement thereto, dated June 20, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Wei Gao and Junming Wu <sup>(3)</sup> ; the No. 3 Supplemental Agreement thereto, dated November 24, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Junming Wu, Lei Zhang and Shizhou Shen <sup>(3)</sup> ; and the No. 4 Supplemental Agreement thereto, dated July 11, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang <sup>(6)</sup> .   |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.23 <sup>(1)</sup> | Power of Attorney, dated September 1, 2005, of Novel-Tongfang Information Engineering Co., Ltd.  |
| 4.24 <sup>(1)</sup> | Power of Attorney, dated August 18, 2007, of Wei Gao.  |
| 4.25 <sup>(3)</sup> | Power of Attorney, dated June 20, 2008, of Junming Wu.   |
| 4.26 <sup>(3)</sup> | Power of Attorney, dated November 24, 2008, of Shizhou Shen.   |
| 4.27 <sup>(3)</sup> | Power of Attorney, dated November 24, 2008, of Lei Zhang.  |
| 4.28 <sup>(1)</sup> | Entrusted Loan Agreement, dated August 23, 2004, among Beijing Super TV Co., Ltd., Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.29 <sup>(1)</sup> | Entrusted Loan Agreement, dated July 13, 2004, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.30 <sup>(1)</sup> | Entrusted Loan Agreement, dated August 25, 2005, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.31 <sup>(1)</sup> | Loan Agreement, dated April 4, 2007, between Beijing Super TV Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd. and the related Entrusted Loan Agreement, dated April 12, 2007, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Bank of Beijing, Shangdi Branch. |
| 4.32 <sup>(3)</sup> | Loan Agreement, dated November 24, 2008, between Shizhou Shen and Beijing Super TV Co., Ltd.   |
| 4.33 <sup>(3)</sup> | Loan Agreement, dated November 24, 2008, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.34 <sup>(1)</sup> | Service Agreement, dated April 2, 2007, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd.  |
| 4.35 <sup>(1)</sup> | Interest Payment Agreement, dated November 30, 2006, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.36 <sup>(1)</sup> | Form of Property Lease Agreement.  |
| 4.37 <sup>(1)</sup> | Fixed Assets Transfer Agreement, dated March 28, 2007, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.38 <sup>(1)</sup> | Form of Employment Agreement and related Form of Agreement on Confidentiality and Intellectual Property.   |
| 4.39 <sup>(1)</sup> | Form of Non-Disclosure, Non-Competition, Commitment and Proprietary Information Agreement.   |
| 4.40 <sup>(1)</sup> | Form of Indemnification Agreement for Directors.   |
| 4.41 <sup>(1)</sup> | Amended and Restated 2005 Stock Incentive Plan of China Digital TV Holding Co., Ltd. and form of share option agreement.   |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.42 <sup>(1)</sup> | Cooperation Agreement, dated January 5, 2007, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Jiangsu Qingda Science and Technology Industries Co., Ltd.                          |
| 4.43 <sup>(1)</sup> | Cooperation Agreement, dated July 18, 2007, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and China Electronics Smart Card Co., Ltd.  |
| 4.44 <sup>(1)</sup> | 2008 Stock Incentive Plan of China Digital TV Holding Co., Ltd.  |
| 4.45 <sup>(2)</sup> | Agreement for Equity Transfer of Beijing Novel-Super Digital TV Technology Co., Ltd., dated December 2007, between China Digital TV Technology Co., Ltd. and Golden Benefit Technology Co., Ltd.     |
| 4.46 <sup>(3)</sup> | Intellectual Property Transfer Agreement, dated August 13, 2008, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.47 <sup>(3)</sup> | Equity Transfer Agreement, dated October 5, 2008, between Beijing Super TV Co., Ltd. and Beijing Novel-Super Digital TV Technology Co., Ltd.   |
| 4.48 <sup>(3)</sup> | Framework Agreement for Purchase of Computer Chips, dated December 12, 2008, between Beijing Super TV Co., Ltd. and Beijing Novel-Super Digital TV Technology Co., Ltd.                              |
| 4.49 <sup>(4)</sup> | Framework Agreement for Sale of Software Products, dated July 14, 2009, between Beijing Super TV Co., Ltd. and Beijing Novel-Super Digital TV Technology Co., Ltd.                                   |
| 4.50 <sup>(4)</sup> | Equity Transfer Agreement, dated February 26, 2010, between Beijing Novel-Super Digital TV Technology Co., Ltd. and Beijing Shi Xun Hu Lian Technology Co., Ltd.                                     |
| 4.51 <sup>(5)</sup> | Shareholders Agreement, dated December 1, 2010, between Beijing Super TV Co., Ltd. and Beijing Yuewu Yuntian Software Technology Co., Ltd.   |
| 4.52 <sup>(5)</sup> | Shareholders Agreement, dated April 29, 2011, between Beijing Super TV Co., Ltd. and Beijing Ying Zhi Cheng Technology Co., Ltd.   |
| 4.53 <sup>(5)</sup> | 2010 Stock Incentive Plan of China Digital TV Holding Co., Ltd.  |
| 4.54 <sup>(6)</sup> | Loan Agreement, dated July 11, 2011, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.55 <sup>(6)</sup> | Loan Agreement, dated July 11, 2011, between Tianxing Wang and Beijing Super TV Co., Ltd.  |
| 4.56 <sup>(6)</sup> | Loan Agreement, dated July 11, 2011, between Wenjun Wang and Beijing Super TV Co., Ltd.  |
| 4.57 <sup>(6)</sup> | Capital Increase and Equity Transfer Agreement, dated July 11, 2011, between Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang, Tianxing Wang and Beijing Novel-Super Digital TV Technology Co., Ltd. |
| 4.58 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Lei Zhang.  |
| 4.59 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Shizhou Shen.   |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.60 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Tianxing Wang.  |
| 4.61 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Wenjun Wang.  |
| 4.62 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.63 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Shizhou Shen and Beijing Super TV Co., Ltd.   |
| 4.64 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Tianxing Wang and Beijing Super TV Co., Ltd.  |
| 4.65 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Wenjun Wang and Beijing Super TV Co., Ltd.  |
| 4.66 <sup>(6)</sup> | Written Undertaking, dated November 22, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang.                       |
| 4.67 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Lei Zhang.   |
| 4.68 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Shizhou Shen.  |
| 4.69 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Tianxing Wang.   |
| 4.70 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Wenjun Wang.   |
| 4.71 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Lei Zhang and Beijing Super TV Co., Ltd.   |
| 4.72 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Shizhou Shen and Beijing Super TV Co., Ltd.  |
| 4.73 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Tianxing Wang and Beijing Super TV Co., Ltd.   |
| 4.74 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Wenjun Wang and Beijing Super TV Co., Ltd.   |
| 4.75 <sup>(6)</sup> | Supplemental Agreement to Loan Agreements, dated January 16, 2012, among Beijing Super TV Co., Ltd., Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang.   |
| 4.76 <sup>(6)</sup> | Supplemental Agreement, dated February 9, 2012, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang.                     |
| 4.77 <sup>(6)</sup> | Cooperation Termination Agreement, dated November 9, 2011, between Dongguan SuperTV Video Info Co., Ltd. and the Dongguan branch of the Guangdong Broadcasting TV Network Co., Ltd.                                |
| 4.78 <sup>(6)</sup> | Capital Increase Agreement, dated May 24, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Ying Zhi Cheng Technology Co., Ltd. and Beijing Joysee Technology Co., Ltd. |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.79 <sup>(6)</sup> | First Amendment to First Amended and Restated Shareholders Agreement of China Digital TV Holding Co., Ltd., dated June 14, 2011, among China Digital TV Technology Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., China Cast Investment Holdings Limited, SB Asia Infrastructure Fund L.P., Capital International Private Equity Fund IV, L.P., CGPE IV, L.P. and certain other shareholders. |
| 4.80                | China Digital TV Holding Co., Ltd. 2012 Stock Incentive Plan.  |
| 4.81                | Second Supplemental Agreement to Loan Agreement, dated April 12, 2013, between Beijing Super TV Co., Ltd. and Tianxing Wang.   |
| 8.1                 | List of Subsidiaries of China Digital TV Holding Co., Ltd.   |
| 11.1 <sup>(1)</sup> | Code of Business Conduct and Ethics of China Digital TV Holding Co., Ltd.  |
| 12.1                | CEO Certification pursuant to Rule 13a-14(a).  |
| 12.2                | CFO Certification pursuant to Rule 13a-14(a).  |
| 13.1                | CEO Certification pursuant to Rule 13a-14(b).  |
| 13.2                | CFO Certification pursuant to Rule 13a-14(b).  |
| 23.1                | Consent of Deloitte Touche Tohmatsu Certified Public Accountants LLP.  |
| 23.2                | Consent of Han Kun, PRC Lawyers.   |

Portions of the agreement have been omitted pursuant to a confidential treatment request and have been filed with the SEC separately with a confidential treatment request.

- (1) Previously filed as an exhibit to the Registration Statement on Form F-1 (File No. 333-146072) of China Digital TV Holding Co., Ltd. and incorporated herein by reference thereto.
- (2) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on June 18, 2008 and incorporated herein by reference thereto.
- (3) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on May 20, 2009 and incorporated herein by reference thereto.
- (4) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on April 30, 2010 and incorporated herein by reference thereto.
- (5) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on May 12, 2011 and incorporated herein by reference thereto.
- (6) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on April 17, 2012 and incorporated herein by reference thereto.

**Table of Contents**

**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

**CHINA DIGITAL TV HOLDING CO., LTD.**

By: /s/ Jianhua Zhu

Name: Jianhua Zhu

Title: Chairman and Chief Executive Officer

Date: April 16, 2013

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

| CONTENTS  | PAGE(S)     |
|---|-------------|
| <u>REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM</u>  | F-2         |
| <u>CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2011 AND 2012</u>   | F-3 - F-4   |
| <u>CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012</u> | F-5         |
| <u>CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012</u>    | F-6         |
| <u>CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012</u>           | F-7         |
| <u>NOTES TO CONSOLIDATED FINANCIAL STATEMENTS</u>   | F-8 - F-71  |
| <u>ADDITIONAL INFORMATION-FINANCIAL STATEMENT SCHEDULE I</u>  | F-72 - F-75 |

F-1

**Table of Contents**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

TO THE BOARD OF DIRECTORS AND SHAREHOLDERS OF

CHINA DIGITAL TV HOLDING CO., LTD.

We have audited the accompanying consolidated balance sheets of China Digital TV Holding Co., Ltd. (the Company), its subsidiaries, and its variable interest entity (the VIE) and the VIE's subsidiaries (collectively, the Group) as of December 31, 2011 and 2012, and the related consolidated statements of comprehensive income, changes in equity, and cash flows for each of the three years in the period ended December 31, 2012. Our audits also included the financial statement schedule included in Schedule I. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as of December 31, 2011 and 2012, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

As discussed in Note 2 to the consolidated financial statements, such statements have been adjusted for the retrospective application of the authoritative guidance regarding the presentation of comprehensive income, which was adopted by the Group on January 1, 2012.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Group's internal control over financial reporting as of December 31, 2012, based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 16, 2013 expressed an unqualified opinion on the Group's internal control over financial reporting.

/s/ Deloitte Touche Tohmatsu Certified Public Accountants LLP

Beijing, the People's Republic of China

April 16, 2013

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****CONSOLIDATED BALANCE SHEETS**

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

|   | As of December 31, |                   |
|---|--------------------|-------------------|
|   | 2011               | 2012              |
| <b>ASSETS</b>   |                    |                   |
| Current assets:   |                    |                   |
| Cash and cash equivalents   | \$ 201,557         | \$ 130,697        |
| Restricted cash   | 55,679             | 18                |
| Notes receivable  | 9,168              | 4,101             |
| Accounts receivable, net of allowance for doubtful accounts of \$845 and \$2,223 as of December 31, 2011 and 2012, respectively   | 31,030             | 38,283            |
| Inventories   | 3,918              | 5,678             |
| Prepaid expenses and other current assets   | 6,768              | 5,245             |
| Deferred costs-current  | 524                | 299               |
| Deferred tax assets-current   | 1,352              | 1,503             |
| <b>Total current assets</b>   | <b>309,996</b>     | <b>185,824</b>    |
| Property and equipment, net   | 1,751              | 1,630             |
| Intangible assets, net  | 450                | 198               |
| Goodwill  | 541                | 547               |
| Equity method investments   | 7,766              | 4,268             |
| Deferred costs-non-current  | 379                | 301               |
| Deferred tax assets-non-current   | 455                | 797               |
| <b>Total assets</b>   | <b>\$ 321,338</b>  | <b>\$ 193,565</b> |
| <b>TOTAL LIABILITIES AND EQUITY</b>   |                    |                   |
| Current liabilities:  |                    |                   |
| Short-term loan (of which nil and nil as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)  | 55,193             |                   |
| Accounts payable (of which \$1,222 and \$1,111 as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                               | 1,487              | 1,215             |
| Accrued expenses and other current liabilities (of which \$3,754 and \$4,795 as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively) | 9,313              | 12,305            |
| Deferred revenue-current (of which \$6,005 and \$5,332 as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                       | 7,745              | 7,473             |
| Dividend payable (of which nil and nil as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                                       | 33,172             | 76,999            |
| Income tax payable (of which \$353 and \$89 as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                                  | 1,902              | 3,476             |
| Deferred tax liabilities current (of which nil and nil as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                       |                    | 4,812             |
| <b>Total current liabilities</b>  | <b>108,812</b>     | <b>106,280</b>    |
| Deferred revenue-non-current (of which \$401 and \$255 as of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                       | 401                | 255               |
| Government subsidies (of which nil and \$1,477 of December 31, 2011 and 2012 belonging to the consolidated VIE and VIE s subsidiaries without recourse to the Company, respectively)                                  | 1,803              | 3,867             |

|                   |         |         |
|-------------------|---------|---------|
| Total Liabilities | 111,016 | 110,402 |
|-------------------|---------|---------|

F-3

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****CONSOLIDATED BALANCE SHEETS continued**

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

|   | As of December 31, |            |
|---|--------------------|------------|
|   | 2011               | 2012       |
| Commitments (Note 23)   |                    |            |
| Equity:   |                    |            |
| China Digital TV Holding Co., Ltd. shareholders' equity:  |                    |            |
| Ordinary shares (\$0.0005 par value; 200,000,000 and 200,000,000 shares authorized, 58,981,890 and 59,100,754 shares issued and outstanding as of December 31, 2011 and 2012, respectively) | 29                 | 30         |
| Additional paid-in capital  | 126,583            | 29,724     |
| Statutory reserve   | 17,694             | 17,856     |
| Retained earnings   | 36,401             | 6,765      |
| Accumulated other comprehensive income  | 25,735             | 26,083     |
| Total China Digital TV Holding Co., Ltd. shareholders' equity.  | 206,442            | 80,458     |
| Noncontrolling interest   | 3,880              | 2,705      |
| Total equity  | 210,322            | 83,163     |
| TOTAL LIABILITIES AND EQUITY  | \$ 321,338         | \$ 193,565 |

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

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

|  | For the years ended December 31, |                |               |
|--|----------------------------------|----------------|---------------|
|  | 2010                             | 2011           | 2012          |
| <b>Revenues</b>  |                                  |                |               |
| Products   | \$ 82,518                        | \$ 95,162      | \$ 85,319     |
| Services   | 5,225                            | 5,378          | 4,925         |
| <b>Total revenues</b>  | <b>87,743</b>                    | <b>100,540</b> | <b>90,244</b> |
| Business taxes   | (620)                            | (1,445)        | (1,501)       |
| <b>Net revenues</b>  | <b>87,123</b>                    | <b>99,095</b>  | <b>88,743</b> |
| <b>Cost of revenues (including share-based compensation of \$10, \$52 and \$5 for 2010, 2011 and 2012, respectively)</b>             |                                  |                |               |
| Products   | 15,148                           | 16,100         | 16,880        |
| Services   | 3,040                            | 3,027          | 3,952         |
| <b>Total cost of revenues</b>  | <b>18,188</b>                    | <b>19,127</b>  | <b>20,832</b> |
| <b>Gross profit</b>  | <b>68,935</b>                    | <b>79,968</b>  | <b>67,911</b> |
| <b>Operating expenses:</b>   |                                  |                |               |
| Research and development (including share-based compensation of \$393, \$1,025, and \$552 for 2010, 2011 and 2012, respectively)     | 10,432                           | 13,140         | 17,402        |
| Selling and marketing (including share-based compensation of \$384, \$633 and \$356 for 2010, 2011 and 2012, respectively)           | 8,504                            | 12,377         | 13,606        |
| General and administrative (including share-based compensation of \$691, \$3,852, and \$1,701 for 2010, 2011 and 2012, respectively) | 6,389                            | 9,723          | 9,444         |
| <b>Total operating expenses</b>  | <b>25,325</b>                    | <b>35,240</b>  | <b>40,452</b> |
| <b>Income from operations</b>  | <b>43,610</b>                    | <b>44,728</b>  | <b>27,459</b> |
| Interest income  | 5,294                            | 6,810          | 6,318         |
| Interest expense   |                                  | (1,452)        | (739)         |
| Gain/(loss) from forward contract  |                                  | 404            | (690)         |
| Impairment loss on long-term investments   | (5,000)                          |                | (4,487)       |
| Other (expense)/income   | (92)                             | 594            | 549           |
| <b>Income before income taxes</b>  | <b>43,812</b>                    | <b>51,084</b>  | <b>28,410</b> |
| <b>Income tax expenses/(benefits):</b>   |                                  |                |               |
| Income tax-current   | 10,714                           | 10,344         | 18,035        |
| Income tax-deferred  | (464)                            | (582)          | 4,197         |
| <b>Total income tax expenses</b>   | <b>10,250</b>                    | <b>9,762</b>   | <b>22,232</b> |
| <b>Net income before income from equity method investments</b>   | <b>33,562</b>                    | <b>41,322</b>  | <b>6,178</b>  |

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|  |            |            |            |
|--|------------|------------|------------|
| Loss from equity method investments, net of income taxes   | (151)      | (1,052)    | (640)      |
| Net income   | 33,411     | 40,270     | 5,538      |
| Net loss attributable to noncontrolling interest   | 10         | 730        | 1,389      |
| Net income attributable to China Digital TV Holding Co., Ltd.                                    | \$ 33,421  | \$ 41,000  | \$ 6,927   |
| Net income per share attributable to ordinary shareholders of China Digital TV Holding Co., Ltd. |            |            |            |
| Basic  | \$ 0.57    | \$ 0.70    | \$ 0.12    |
| Diluted  | \$ 0.57    | \$ 0.69    | \$ 0.12    |
| Net income   | \$ 33,411  | \$ 40,270  | \$ 5,538   |
| Other comprehensive income, net of tax   |            |            |            |
| Foreign currency translation adjustment  | 6,943      | 12,175     | 536        |
| Comprehensive income   | 40,354     | 52,445     | 6,074      |
| Comprehensive loss attributable to noncontrolling interest                                       | 10         | 730        | 1,201      |
| Comprehensive income attributable to ordinary shareholders of China Digital TV Holding Co., Ltd  | \$ 40,364  | \$ 53,175  | \$ 7,275   |
| Weighted average shares used in calculating net income per ordinary share                        |            |            |            |
| Basic  | 58,313,467 | 58,934,912 | 59,011,396 |
| Diluted  | 58,779,027 | 59,075,466 | 59,092,804 |

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

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

|  | China Digital TV Holding Co., Ltd. Shareholders |        |                            |  |                   |                   | Total China Digital TV Holding Co., Ltd |                          | Total equity |
|--|---|--------|----------------------------|--|-------------------|-------------------|---|--------------------------|--------------|
|  | Ordinary  |        | Additional paid-in capital | Accumulated other comprehensive income | Statutory reserve | Retained earnings | Shareholders equity                     | Non-controlling Interest |              |
|  | Shares  | Amount |                            |  |                   |                   |   |                          |              |
| Balance at January 1, 2010                       | 58,044,640                                      | \$ 29  | \$ 157,980                 | \$ 6,617                               | \$ 12,691         | \$ 75,707         | \$ 253,024                              | \$                       | \$ 253,024   |
| Share-based compensation                         |   |        | 1,478                      |  |                   |                   | 1,478                                   |                          | 1,478        |
| Provision for statutory reserve                  |   |        |                            |  | 4,633             | (4,633)           |   |                          |              |
| Exercise of stock option                         | 773,347   |        | 1,270                      |  |                   |                   | 1,270                                   |                          | 1,270        |
| Special cash dividend to shareholders            |   |        | (41,929)                   |  |                   | (75,707)          | (117,636)                               |                          | (117,636)    |
| Noncontrolling interest of Dongguan Super TV     |   |        |                            |  |                   |                   |   | 530                      | 530          |
| Net income                                       |   |        |                            |  |                   | 33,421            | 33,421                                  | (10)                     | 33,411       |
| Foreign currency translation adjustment          |   |        |                            | 6,943                                  |                   |                   | 6,943                                   |                          | 6,943        |
| Balance at December 31, 2010                     | 58,817,987                                      | 29     | 118,799                    | 13,560                                 | 17,324            | 28,788            | 178,500                                 | 520                      | 179,020      |
| Share-based compensation                         |   |        | 5,562                      |  |                   |                   | 5,562                                   |                          | 5,562        |
| Provision for statutory reserve                  |   |        |                            |  | 370               | (370)             |   |                          |              |
| Exercise of stock option                         | 163,903   |        | 400                        |  |                   |                   | 400                                     |                          | 400          |
| Special cash dividend to shareholders            |   |        |                            |  |                   | (33,017)          | (33,017)                                |                          | (33,017)     |
| Disposal of Dongguan Super TV                    |   |        |                            |  |                   |                   |   | (625)                    | (625)        |
| Capital injection by noncontrolling shareholders |   |        |                            |  |                   |                   |   | 6,537                    | 6,537        |
| Transfer of noncontrolling interest              |   |        | 1,822                      |  |                   |                   | 1,822                                   | (1,822)                  |              |
| Net income                                       |   |        |                            |  |                   | 41,000            | 41,000                                  | (730)                    | 40,270       |
| Foreign currency translation adjustment          |   |        |                            | 12,175                                 |                   |                   | 12,175                                  |                          | 12,175       |
| Balance at December 31, 2011                     | 58,981,890                                      | 29     | 126,583                    | 25,735                                 | 17,694            | 36,401            | 206,442                                 | 3,880                    | 210,322      |
| Share-based compensation                         |   |        | 2,588                      |  |                   |                   | 2,588                                   | 26                       | 2,614        |
| Provision for statutory reserve                  |   |        |                            |  | 162               | (162)             |   |                          |              |
| Exercise of stock option                         | 118,864   | 1      | 85                         |  |                   |                   | 86                                      |                          | 86           |
| Special cash dividend to shareholders            |   |        | (99,532)                   |  |                   | (36,401)          | (135,933)                               |                          | (135,933)    |
| Net income                                       |   |        |                            |  |                   | 6,927             | 6,927                                   | (1,389)                  | 5,538        |
| Foreign currency translation adjustment          |   |        |                            | 348                                    |                   |                   | 348                                     | 188                      | 536          |
| Balance at December 31, 2012                     | 59,100,754                                      | \$ 30  | \$ 29,724                  | \$ 26,083                              | \$ 17,856         | \$ 6,765          | \$ 80,458                               | \$ 2,705                 | \$ 83,163    |

The accompanying notes are an integral part of these consolidated financial statements.



**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

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

|   | For the years ended December 31, |           |          |
|---|----------------------------------|-----------|----------|
|   | 2010                             | 2011      | 2012     |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                                  |           |          |
| Net income  | \$ 33,411                        | \$ 40,270 | \$ 5,538 |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                  |           |          |
| Depreciation and amortization   | 1,272                            | 1,343     | 1,174    |
| Share-based compensation  | 1,478                            | 5,562     | 2,614    |
| Loss/(gain) from disposal of property and equipment                               | 18                               | (297)     |          |
| Allowance for doubtful accounts   | 182                              | 87        | 1,378    |
| Provision for inventory   | 35                               | 45        | 217      |
| Warranty accrual  | 81                               | 84        | 69       |
| Loss from equity method investments   | 151                              | 1,052     | 640      |
| (Income)/loss from deconsolidation of a subsidiary                                | (32)                             | 129       |          |
| Impairment loss of an intangible asset  | 20                               |           |          |
| Impairment loss on long-term investments  | 5,000                            |           | 4,487    |
| Gain from disposal of cost method investment                                      |                                  |           | (820)    |
| Interest income in held-to-maturity securities                                    | (1,218)                          | (319)     |          |
| (Gain)/loss from forward contract   |                                  | (404)     | 690      |
| Changes in assets and liabilities:  |                                  |           |          |
| Accounts receivable and notes receivable  | (11,692)                         | (13,684)  | (3,105)  |
| Inventories   | 1,767                            | (967)     | (1,967)  |
| Prepaid expenses and other current assets   | (2,360)                          | (73)      | (81)     |
| Deferred cost   | (56)                             | (65)      | 309      |
| Accounts payable  | 790                              | 3         | (284)    |
| Income tax payable  | (1,385)                          | 1,768     | 1,535    |
| Accrued expenses and other current liabilities                                    | 3,298                            | 465       | 2,770    |
| Deferred revenue  | 2,277                            | 1,465     | (483)    |
| Government subsidies  |                                  | 1,803     | 2,019    |
| Deferred income taxes   | (464)                            | (582)     | 4,197    |
| Net cash provided by operating activities   | 32,573                           | 37,685    | 20,897   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                      |                                  |           |          |
| Purchase of property and equipment  | (606)                            | (694)     | (783)    |
| Bank deposits maturing over three months  | 25,041                           | 41,667    |          |
| Restricted cash   |                                  | (55,663)  | 55,530   |
| Interest income from held-to-maturity securities                                  | 1,364                            | 677       |          |
| Purchase of held-to-maturity corporate and the PRC government bonds               | (24,770)                         |           |          |
| Proceeds from maturity of held to maturity corporate and the PRC government bonds | 37,841                           | 26,626    |          |
| Cash in a deconsolidated entity   |                                  | (1,963)   |          |
| Cash in an acquired entity  | 922                              |           |          |
| Proceeds from disposal of property and equipment                                  | 152                              | 543       |          |
| Proceeds from disposal of Dongguan Super TV                                       |                                  |           | 1,046    |
| Proceeds from disposal of cost method investment                                  |                                  |           | 820      |
| Purchase of equity method investment  | (8,500)                          |           | (1,588)  |
| Purchase of cost method investment  | (5,000)                          |           |          |
| Deposit for investment in Cyber Cloud   | (6,818)                          |           |          |
| Refund of deposit for investment in Cyber Cloud                                   |                                  | 6,818     |          |

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|  |                |                |                 |
|--|----------------|----------------|-----------------|
| Net cash provided by investing activities                    | 19,626         | 18,011         | 55,025          |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                 |                |                |                 |
| Proceeds from stock option exercise                          | 1,270          | 400            | 85              |
| Short-term loan  |                | 55,193         | (55,193)        |
| Capital injection by noncontrolling shareholders             |                | 6,537          |                 |
| Special cash dividend paid to shareholders                   | (40,303)       | (77,178)       | (92,106)        |
| Net cash used in financing activities                        | (39,033)       | (15,048)       | (147,214)       |
| Effect of exchange rate changes on cash and cash equivalents | 4,691          | 11,965         | 432             |
| <b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>  | <b>17,857</b>  | <b>52,613</b>  | <b>(70,860)</b> |
| CASH AND CASH EQUIVALENTS, BEGINNING OF THE YEAR             | 131,087        | 148,944        | 201,557         |
| <b>CASH AND CASH EQUIVALENTS, END OF THE YEAR</b>            | <b>148,944</b> | <b>201,557</b> | <b>130,697</b>  |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>      |                |                |                 |
| Income tax paid  | 6,680          | 8,194          | 6,934           |
| Withholding tax paid   | 5,380          |                | 9,554           |
|  | \$ 12,060      | \$ 8,194       | \$ 16,488       |
| <b>Non-cash investing and financing activities</b>           |                |                |                 |
| Acquisition of equity interest                               | \$ 262         | \$             | \$              |
| Receivable on disposal of Dongguan Super TV                  | \$             | \$ 1,046       | \$              |
| Dividend payable   | \$ 77,333      | \$ 33,172      | \$ 76,999       |

The accompany notes are an integral part of these consolidated financial statements.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES**

China Digital TV Technology Co., Ltd. ( CDTV BVI ) was incorporated in the British Virgin Islands ( BVI ) as a limited liability company on March 9, 2004 by the shareholders of Novel-Tongfang Information Engineering Co., Ltd. ( N-T Information Engineering ) and SB Asia Infrastructure Fund L.P. ( SAIF ), a third-party investor. The principal activities of CDTV BVI are to install and integrate conditional access systems ( CA Systems ), subscriber management systems and electronic program guidance systems to cable TV operators in the People's Republic of China ( PRC ) and to sell digital TV intelligent cards ( smart cards ) to these operators.

The development, production and sale of commercial encryption products in the PRC are regulated by the PRC National Encryption Administrative Bureau. Currently, foreign-invested enterprises incorporated in the PRC are not expressly prohibited from conducting encryption-related businesses; however, they may have difficulty in obtaining the licenses or permits required for conducting such businesses from the Encryption Bureau due to the PRC Encryption Authority's generally restrictive approach towards foreign participation in the PRC encryption industry. In addition, the PRC State Administration of Radio, Film and Television ( SARFT ) has a policy to require any cable television network operator who uses non-PRC CA systems to install parallel PRC CA systems. Such policy does not expressly indicate whether the CA systems produced by a foreign-invested company incorporated in the PRC fall into the category of non-PRC CA systems. In consideration of the PRC Encryption Authority's preferences and the SARFT's policy, CDTV BVI conducts substantially all of its operations through its subsidiary, Beijing Super TV Co., Ltd. ( Super TV ), and Novel-Tongfang Digital TV Technology Co., Ltd. ( N-T Digital TV ), a variable interest entity ( VIE ), which is 100% owned by PRC citizens and has obtained the license to operate such business in the PRC.

N-T Digital TV was established in the PRC on May 31, 2004 by N-T Information Engineering (who contributed 75% of the paid-in capital) and Ms. Li Yang, who is a PRC citizen representing SAIF (which contributed 25% of the paid-in capital). N-T Digital TV was subsequently renamed to Beijing Novel-Super Digital TV Technology Co., Ltd. ( N-S Digital TV ) in December 2007. In August 2007, Ms. Li Yang transferred her entire equity interest in the VIE to Ms. Wei Gao, a PRC citizen representing SAIF. In June 2008, Ms. Wei Gao transferred her entire equity interest in the VIE to Mr. Junming Wu, a PRC citizen employed by Super TV and the business registration was completed in 2009. In November 2008, N-T Information Engineering transferred its entire equity interest in the VIE to Mr. Lei Zhang and Mr. Shizhou Shen, two PRC citizens employed by Super TV. In July 2011, Mr. Junming Wu transferred his entire equity interest in the VIE to Mr. Tianxing Wang. Meanwhile, Mr. Lei Zhang, Mr. Tianxing Wang and Mr. Wenjun Wang, all of whom are PRC citizens employed by Super TV, contributed cash to increase the registered capital of the VIE by \$18,170 using the loans proceeds from Super TV. After these transactions, the VIE is owned by Mr. Shizhou Shen, Mr. Lei Zhang, Mr. Tianxing Wang and Mr. Wenjun Wang with equity interest of 8.3%, 31.6%, 31.2% and 28.9%, respectively. CDTV BVI does not have direct equity interest in the VIE, but it obtains control and enjoys the economic benefits of the VIE through a series of contractual arrangements entered into among Super TV, the VIE and its equity holders.

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**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued**

In 2007, the shareholders of CDTV BVI established China Digital TV Holding Co., Ltd. (the Company or CDTV Holding ), as the holding Company of CDTV BVI and its subsidiary and VIE, CDTV Holding was incorporated in the Cayman Islands. The shareholders of CDTV BVI exchanged all of their shares of CDTV BVI for shares of CDTV Holding in proportion to their percentage interests in CDTV BVI. As a result, CDTV BVI became a wholly owned subsidiary of CDTV Holding.

***VIE contractual agreements***

A majority of the Group's customers are provincial and municipal cable network operators in the PRC, which are primarily state-owned enterprises ( SOEs ). Due to the above-mentioned regulatory considerations, these SOEs tend to purchase CA systems from PRC local companies, rather than from companies with foreign investment such as Super TV. In order to accommodate the PRC regulations and participate in the smart card and CA systems business (for the benefit of the Group), the Group arranged for Super TV to enter into the following agreements with the VIE and its equity holders:

**Technical Support and Related Services Agreement:** Super TV exclusively provides the VIE and/or its customers with technical support, technical training and personnel services relating to the VIE's marketing activities and services relating to the maintenance and optimization for the products and software of the VIE's customers at the VIE's request. The fees for such technical support and services are determined at Super TV's discretion. The term of this agreement is 15 years, which may not be terminated prior to its termination date without Super TV's written consent. The term of this agreement will be automatically renewed for another 15 years upon its expiration date unless written notice has been given by Super TV.

**Technology License Agreement:** The VIE granted Super TV, free of charge, an exclusive license to use certain software copyrights, patents, unpatentable technology and technical secrets relating to the digital television business that was transferred from N-T Information Engineering to the VIE. The term of the license is ten years, which may not be terminated or amended without the written consent of Super TV prior to its termination date and will be automatically renewed for an additional ten years upon its termination date unless written notice has been given by Super TV.

Table of Contents

CHINA DIGITAL TV HOLDING CO., LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)

1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued

*VIE contractual agreements* continued

**Technology Development Agreement:** The VIE engaged Super TV to develop all technology required by the VIE or its customers. The fees payable by the VIE to Super TV under the agreement will be based on the price and quantity of the technology products, and a set percentage determined by Super TV. The term of the agreement is ten years, which may not be terminated prior to its termination date without Super TV's written consent. The term of this agreement will be automatically renewed for an additional ten years upon its termination date unless written notice has been given by Super TV.

**Products and Software Purchase Agreement:** The VIE purchased from Super TV all the smart cards and related software products required for its CA systems. The purchase price is determined by Super TV. The term of the agreement is 15 years, which may not be terminated prior to its termination date without Super TV's written consent. The term of this agreement will be automatically renewed for an additional 15 years upon its termination date unless written notice has been given by Super TV.

**Business Operating Agreement:** Each of the Shareholders agreed to (i) accept the policies and guidelines furnished by Super TV with respect to the hiring and dismissal of employees, operational management and financial management systems of the VIE; (ii) appoint the candidates recommended by Super TV as directors of the VIE and appoint the senior management personnel of Super TV as the general manager, chief financial officer and other senior officers of the VIE based on Super TV's recommendations; (iii) replace or remove any director or senior management personnel of the VIE upon Super TV's request; and (iv) seek a guarantee from Super TV first when any guarantee is required to secure performance by the VIE of any contract or working capital loan borrowed by the VIE and pledge its assets and receivables to Super TV as a counter-guarantee. This agreement has a term of ten years and may be renewed at the option of Super TV by giving written notice for a term to be determined by Super TV. Super TV may terminate this agreement at any time by giving 30 days' advance written notice to the other parties to this agreement.

**Loan agreements:** Under loan agreements between Super TV and the registered shareholders of the VIE, Super TV extended loans to the registered shareholders of the VIE for contributing registered capital to the VIE in order to hold 100% of the equity interest in the VIE. The term of each loan is ten years, which is automatically renewable for another ten years upon its termination date unless a written notice has been provided by Super TV one month prior to such termination date. The registered shareholders of the VIE may not repay the loan prior to the termination date of the relevant loan agreement, unless so requested by Super TV, and may only repay the loan by (i) transferring all his equity interests in the VIE to Super TV or any third party designated by Super TV and (ii) paying Super TV with the entire proceeds obtained by himself from such transfer.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued**

*VIE contractual agreements* continued

**Share Pledge Agreements:** Pursuant to the share pledge agreements, each of the Shareholders pledged all of their respective equity interests in the VIE to Super TV to secure the Shareholders' and the VIE's performance of their respective obligations under the VIE contractual arrangements between the VIE/the Shareholders and Super TV. In addition, each of the Shareholders agreed not to transfer their equity interests in the VIE or create, or allow the creation of, any pledge over their respective equity interests in the VIE that may affect Super TV's interests without Super TV's consent. Super TV is entitled to receive the dividends on the pledged equity interests during the term of the pledges. The duration of each of the share pledge agreements is equivalent to the maximum duration of the VIE contractual arrangements between the VIE/the Shareholders and Super TV. The agreements may only be terminated: (i) by Super TV in writing; or (ii) upon the fulfillment of the Shareholders' and the VIE's respective obligations under the VIE contractual arrangements between the VIE/the Shareholders and Super TV, which is subject to Super TV's written confirmation.

**Powers of Attorney:** Each of the Shareholders has executed an irrevocable power of attorney appointing Super TV, or any person designated by Super TV, as the attorney-in-fact to vote on their respective behalves on all matters of the VIE requiring shareholder approval under PRC laws, rules and regulations and the articles of association of the VIE. Each power of attorney has a term of ten years, subject to earlier termination in the event of the termination of the relevant share pledge agreement. The powers of attorney will be automatically renewed upon the extension of the term of the relevant share pledge agreement.

**Equity Transfer Option Agreement:** Under this agreement, Mr. Lei Zhang, Mr. Shizhou Shen, Mr. Wenjun Wang and Mr. Tianxing Wang (the Shareholders) jointly granted Super TV an exclusive and irrevocable option to purchase all of the equity interests held by them in the VIE at any time that Super TV deems fit. Super TV may purchase these equity interests itself or designate another party to purchase the equity interests. The exercise price of the option will be determined by Super TV or its designated third party at the time of the exercise, subject to the minimum purchase price requirements pursuant to applicable PRC law or otherwise permitted by the relevant PRC authorities. This agreement does not have a specified term and will remain in effect unless terminated with the written consent of Super TV.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued**

*VIE contractual agreements* continued

As a result of these contractual arrangements, Super TV (1) has the power to direct the activities that most significantly affects the economic performance of the VIE, and (2) receives the economic benefits of the VIE. Accordingly, the Company is considered the primary beneficiary of the VIE and has consolidated the VIE's financial results of operations, assets and liabilities in the Company's consolidated financial statements. In making the conclusion that the Company is the primary beneficiary of the VIE, the Company believes the Company's rights under the terms of the equity transfer option agreement provide it with a substantive kick out right. More specifically, the Company believes the terms of the equity transfer option agreement are valid, binding and enforceable under PRC laws and regulations currently in effect. The Company also believes that the minimum amount of consideration permitted by the applicable PRC law to exercise the option does not represent a financial barrier or disincentive for the Company to currently exercise its rights under the equity transfer option agreement. In addition, the articles of association of VIE provides that the shareholders of VIE have the power to, in a shareholders' meeting: (i) approve the operating strategy and investment plan; (ii) elect the members of board of directors and approve their compensation; and (iii) review and approve the annual budget and earnings distribution plan. Consequently, the Company's rights under the powers of attorney reinforce the Company's abilities to direct the activities that most significantly impact the VIE's economic performance. The Company also believes that this ability to exercise control ensures that the VIE will continue to execute and renew service agreements and pay service fees to the Company. By charging service fees in whatever amounts the Company deems fit, and by ensuring that service agreements are executed and renewed indefinitely, the Company has the rights to receive substantially all of the economic benefits from the VIE.

***Risks in relation to the VIE structure***

The Company believes that the contractual arrangements with the VIE and its shareholders are in compliance with PRC law and regulations and are legally enforceable. However, uncertainties in the PRC legal system could limit the Company's ability to enforce the contractual arrangements. If the legal structure and contractual arrangements were found to be in violation of PRC laws and regulations, the PRC government could:

- levying fines;
- confiscating income;
- revoking business licenses or operating licenses;
- requiring the Company to revise its ownership structure or restructure its operations;
- requiring the discontinuation of businesses;
- restricting or requiring the Company to discontinue related-party transactions among its PRC subsidiaries, on the one hand, and N-S Digital TV and its subsidiaries, on the other hand;
- limiting the Company's business expansion in China; and/or
- imposing additional conditions or requirements with which the Company may not be able to comply.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued***Risks in relation to the VIE structure* continued

The Company's ability to conduct its business may be negatively affected if the PRC government were to carry out any of the aforementioned actions. As a result, the Company may not be able to consolidate the VIE and its subsidiaries in its financial statements as it may lose the ability to exert effective control over the VIE and its subsidiaries and its shareholders, and it may lose the ability to receive economic benefits from the VIE and its subsidiaries. The Company, however, does not believe such actions would result in the liquidation or dissolution of the Company, the Super TV or the VIE and its subsidiaries.

The shareholders of the VIE are also the employees of the Company. Moreover, certain of the shareholders of the VIE are also the shareholders of the Company. Their interests as beneficial owners of the VIE may differ from the interests of the Company as a whole. The Company cannot assure that when conflicts of interest arise, these parties will act in the best interests of the Company or that conflicts of interests will be resolved in the Company's favor. Currently, the Company does not have existing arrangements to address potential conflicts of interest these parties may encounter in their capacity as beneficial owners of the VIE, on the one hand, and as shareholders and employees of the Company, on the other hand. Through the powers of attorney, the VIE entrusted Super TV as its proxy to exercise its rights as the shareholder of the VIE with respect to an aggregate of 100% of the equity interests in the VIE. The Company believes the shareholders of the VIE will not act contrary to any of the contractual arrangements and the equity transfer option agreement provides the Company with a mechanism to remove them as shareholders of the VIE should they act to the detriment of the Company. If any conflict of interest or dispute between the Company and the shareholders of the VIE arises and the Company is unable to resolve it, the Company would have to rely on legal proceedings in the PRC. Such legal proceedings could result in disruption of its business; moreover, there is substantial uncertainty as to the ultimate outcome of any such legal proceedings.

The following financial statement amounts and balances of the VIE and VIE's subsidiaries were included in the accompanying consolidated financial statements as of and for the years ended December 31:

|                               | As of December 31, |                  |
|-------------------------------|--------------------|------------------|
|                               | 2011               | 2012             |
| Total current assets          | \$ 52,490          | \$ 57,932        |
| Total non-current assets      | 1,923              | 3,227            |
| <b>Total assets</b>           | <b>\$ 54,413</b>   | <b>\$ 61,159</b> |
| Total current liabilities     | \$ 11,334          | \$ 11,327        |
| Total non-current liabilities | 401                | 1,732            |
| <b>Total liabilities</b>      | <b>\$ 11,735</b>   | <b>\$ 13,059</b> |

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued***Risks in relation to the VIE structure* continued

|                   | For the years ended December 31, |           |           |
|-------------------|----------------------------------|-----------|-----------|
|                   | 2010                             | 2011      | 2012      |
| Net revenues      | \$ 79,591                        | \$ 92,298 | \$ 78,940 |
| Net income/(loss) | \$ 137                           | \$ 3,512  | \$ (837)  |

|   | For the years ended December 31, |          |          |
|---|----------------------------------|----------|----------|
|   | 2010                             | 2011     | 2012     |
| Net cash provided by operating activities | \$ 172                           | \$ 1,880 | \$ 4,464 |
| Net cash used in investing activities     | 1,228                            | (2,026)  | (1,645)  |
| Net cash provided by financing activities | \$                               | \$       | \$       |

The VIE and its subsidiaries contributed an aggregate of 91.4%, 93.1% and 89.0% of the consolidated net revenues for the year ended December 31, 2010, 2011 and 2012, respectively. The Company's business, which is not conducted through contractual arrangements with the VIE, primarily consists of sales of multimedia home entertainment boxes and cloud computing technology-based services. As of the fiscal years ended December 31, 2011 and 2012, the VIE and its subsidiaries accounted for an aggregate of 16.9% and 31.6%, respectively, of the consolidated total assets, and 10.6% and 11.8%, respectively, of the consolidated total liabilities.

There are no consolidated VIE's assets that are collateral for the VIE's obligations and can only be used to settle the VIE's obligations. There are no creditors (or beneficial interest holders) of the VIE that have recourse to the general credit of the Company or any of its consolidated subsidiaries. There are no terms in any arrangements, considering both explicit arrangements and implicit variable interests, that require the Company or its subsidiaries to provide financial support to the VIE. However, if the VIE ever needs financial support, the Company or its subsidiaries may, at its option and subject to statutory limits and restrictions, provide financial support to its VIE through loans to the shareholder of the VIE or entrustment loans to the VIE.

Relevant PRC laws and regulations restrict the VIE from transferring a portion of its net assets, equivalent to the balance of its statutory reserve and its share capital, to the Company in the form of loans and advances or cash dividends. Please refer to Note 26 for disclosure of restricted net assets.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****1. ORGANIZATION AND PRINCIPAL ACTIVITIES continued***Risks in relation to the VIE structure* continued

As of December 31, 2012, CDTV Holding's subsidiaries, VIE and VIE's subsidiaries include the following entities:

|   | Date of incorporation<br>/acquisition | Place of incorporation<br>/establishment | Percentage of<br>economic ownership |
|---|---------------------------------------|--|-------------------------------------|
| <u>Subsidiaries</u>   |                                       |  |                                     |
| CDTV BVI  | March 9, 2004                         | BVI                                      | 100%                                |
| Super TV  | May 31, 2004                          | the PRC                                  | 100%                                |
| Golden Benefit Technology Limited<br>( Golden Benefit )   | December 6, 2007                      | Hong Kong                                | 100%                                |
| China Super Media Holdings Limited<br>( CSM Holdings )  | February 25, 2008                     | Hong Kong                                | 100%                                |
| N-S Investment Holdings Co., Ltd<br>( N-S Investment Holdings )   | July 23, 2010                         | the PRC                                  | 100%                                |
| Beijing Cyber Cloud Co., Ltd.<br>( Cyber Cloud )  | January 19, 2011                      | the PRC                                  | 90%                                 |
| Beijing Joysee Technology Co., Ltd<br>( Joysee )  | May 13, 2011                          | the PRC                                  | 64.8%                               |
| Beijing Super Movie Technology Co.,<br>LTD<br>( Super Movie )   | September 23, 2011                    | the PRC                                  | 90%                                 |
| <u>VIE</u>  |                                       |  |                                     |
| N-S Digital TV  | May 31, 2004                          | the PRC                                  | 100%                                |
| <u>VIE's subsidiaries</u>   |                                       |  |                                     |
| Guangdong Digital Media Technology<br>Research & Development Institute Co.,<br>Ltd<br>( Guangdong R&D ) | February 28, 2010                     | the PRC                                  | 100%                                |
| N-S Media Investment Co., Ltd<br>( N-S Media Investment )   | December 19, 2007                     | the PRC                                  | 100%                                |

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) Basis of presentation**

The consolidated financial statements of the Group have been prepared in accordance with the accounting principles generally accepted in the United States of America ( U.S. GAAP ).

**(b) Basis of consolidation**

The consolidated financial statements of the Group include the financial statements of CDTV Holding, its subsidiaries, VIE and VIE s subsidiaries. All inter-company transactions and balances have been eliminated upon consolidation.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

***(c) Use of estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and revenues, costs and expenses in the financial statements and accompanying notes. Significant accounting estimates reflected in the Group's consolidated financial statements include allowance for doubtful accounts, the useful lives and impairment of property and equipment, useful lives and impairment of intangible assets, allowance for obsolete inventories, valuation allowance for deferred tax assets, impairment of goodwill and impairment of long-term investments.

***(d) Cash and cash equivalents***

Cash and cash equivalents consist of cash on hand and highly liquid investments which are unrestricted as to withdrawal or use, and which have maturities of three months or less when purchased.

***(e) Accounts receivable and allowance for doubtful accounts***

Accounts receivable are stated at the amount the Group expects to collect. The Group maintains allowances for doubtful accounts for estimated losses. Management considers the following factors when determining the collectability of specific accounts: historical experience, credit worthiness of the clients, aging of the receivables and other specific circumstances related to the accounts. Allowance for doubtful accounts is made based on aging of accounts receivable and on any specifically identified accounts receivable that may become uncollectible.

***(f) Investment***

***Held-to-maturity investments***

Investments are classified as held-to-maturity when the Group has the positive intent and ability to hold the debt security to maturity. The difference between the amortized cost basis and the cash flows expected to be collected is accreted as interest income.

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**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(f) Investment* continued

*Equity method investments*

Investee companies over which the Group has the ability to exercise significant influence, but does not have a controlling interest are accounted for using the equity method. Significant influence is generally considered to exist when the Group has an ownership interest in the voting stock of the investee between 20% and 50%, and other factors, such as representation on the investee's Board of Directors, voting rights and the impact of commercial arrangements, are considered in determining whether the equity method of accounting is appropriate.

Investee companies over which the Group has equity interest over 50%, but the noncontrolling shareholders have substantive rights to participate in significant operating decisions are accounted for using the equity method.

An impairment charge is recorded if the carrying amount of the investment exceeds its fair value and this condition is determined to be other-than-temporary. The Group did not incur any impairment loss on equity method investments for the years ended December 31, 2010 and 2011. For the year ended December 31, 2012, the Group incurred impairment loss of \$4,487 on equity method investments (see Note 12 (c)).

*Cost method investments*

Investee companies over which the Group does not have significant influence and a controlling interest, the Group carries the investment at cost and recognizes as income for any dividend received from distribution of the investee's earnings.

An impairment charge is recorded if the carrying amount of the investment exceeds its fair value and determined to be other-than-temporary.

*(g) Financial instruments*

Financial instruments of the Group primarily consist of cash and cash equivalents, restricted cash, held-to-maturity investments, notes receivable, accounts receivable, accounts payable, short term loan, forward contracts. The carrying values of the Group's financial instruments, except for held-to-maturity investments, approximate their fair values, principally because of the short-term maturity of these instruments or their terms. The held-to-maturity investments are stated at amortized cost.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued***(h) Concentration of credit risk*

Financial instruments that potentially expose the Group to concentrations of credit risk consist primarily of cash and cash equivalents, restricted cash and accounts receivable. The Group places their cash and cash equivalents and restricted cash with financial institutions with high-credit ratings and quality.

Approximately 96.7% of the Group's deposits were placed with two commercial banks in the PRC as of December 31, 2012. The Group takes into account a number of factors, including, among other things, the industry rankings, credit rating and reputation, in determining the creditworthiness and quality of the financial institutions in the PRC with which it has placed its cash and cash equivalents, restricted cash and bank deposits maturing over three months. The following table sets forth information relating to the three largest proportions of the Group's total deposits held by a single bank as of December 31, 2011 and 2012, respectively.

Details of the bank accounting for 10% or more of total deposits are as follows:

| Bank   | As of<br>December 31, |      |
|--------|-----------------------|------|
|        | 2011                  | 2012 |
|        | %                     | %    |
| Bank A | 15.6                  | 76.5 |
| Bank B | 57.8                  | 20.2 |
| Bank C | 22.8                  | *    |

The Group conducts credit evaluations of customers and generally does not require collateral or other security from customers. The Group establishes an allowance for doubtful accounts primarily based upon the age of the receivables and factors relevant to determining the credit risk of specific customers.

Details of the customer accounting for 10% or more of total revenues are as follows:

| Customer   | For the years ended<br>December 31, |      |      |
|------------|-------------------------------------|------|------|
|            | 2010                                | 2011 | 2012 |
|            | %                                   | %    | %    |
| Customer A | 14.2                                | *    | *    |

For the years ended December 31, 2011 and 2012, there are no revenues from customers that individually represent greater than 10% of the total revenues.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued****(h) Concentration of credit risk** continued

Details of the customer accounting for 10% or more of accounts receivable are as follows:

| Customer   | As of<br>December 31, |      |
|------------|-----------------------|------|
|            | 2011                  | 2012 |
|            | %                     | %    |
| Customer A | 10.9                  | 10.5 |

\* The amount was less than 10%.

**(i) Inventories**

Inventories are stated at the lower of cost or market value. Cost is determined using the weighted average method. Inventories are written down for provisions for obsolescence to net realizable value based upon estimates of future demand, technology developments, and market conditions.

**(j) Property and equipment, net**

Property and equipment are carried at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated on a straight-line basis over the following estimated useful lives:

|                                   |   |
|-----------------------------------|---|
| Computer and electronic equipment | 3 years   |
| Furniture and fixture             | 5 years   |
| Leasehold improvement             | Shorter of useful life of the asset or the lease term |
| Motor vehicles                    | 5 years   |

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued****(k) Intangible assets, net**

Intangible assets, other than goodwill, resulting from the acquisitions of entities accounted for using the acquisition method of accounting are estimated by management based on the fair value of assets acquired.

Identifiable intangible assets are carried at cost less accumulated amortization. Amortization of finite-lived intangible assets is computed using the straight-line method over the following estimated average useful lives, which are as follows:

|                                 |           |
|---------------------------------|-----------|
| Core technology                 | 7.5 years |
| Complete technology             | 2.5 years |
| Contract backlogs               | 1 year    |
| Customer relationship           | 3.5 years |
| Digital watermarking technology | 5 years   |
| Image tracing technology        | 5 years   |

**(l) Impairment of long-lived assets**

Long-lived assets, such as property and equipment and definite-lived intangible assets are stated at cost less accumulated depreciation or amortization. Depreciation and amortization is computed principally by the straight-line method.

The Group evaluates the recoverability of long-lived assets, including identifiable intangible assets with determinable useful lives whenever events or changes in circumstances indicate that an intangible asset's carrying amount may not be recoverable. The Group measures the carrying amount of long-lived asset against the estimated undiscounted future cash flows associated with it. Impairment exists when the sum of the expected future net cash flows is less than the carrying value of the asset being evaluated.

Impairment loss for the years ended December 31, 2010, 2011 and 2012 was \$20, nil and nil respectively.

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**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

***(m) Goodwill***

The excess of the purchase price over the fair value of net assets acquired is recorded on the consolidated balance sheet 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 on an annual basis 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 the stock prices, business climate, legal factors, operating performance indicators, competition, or sale or disposition of a significant portion of a reporting unit.

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. Estimating fair value is performed by utilizing various valuation techniques, with primary technique being a discounted cash flow which requires significant judgments, including estimation of future cash flows, which is dependent on internal forecasts, estimation of the long term rate of growth for the Company's business, estimation of the useful life over which cash flows will occur, and determination of the Company's weighted average cost of capital.

In September 2011, the FASB issued an authoritative pronouncement related to testing goodwill for impairment. The guidance permits the Company to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The Company adopted this pronouncement since 2012. If it is more likely than not that the fair value of a reporting unit is less than its carrying amount, goodwill is then tested following a two-step process. The first step compares the fair value of each reporting unit to its carrying amount, including goodwill. If the fair value of each reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step will not be required. If the carrying amount of a reporting unit exceeds its fair value, the second step compares the implied fair value of goodwill to the carrying value of a reporting unit's goodwill. The implied fair value of goodwill is determined in a manner similar to accounting for a business combination with the allocation of the assessed fair value determined in the first step to the assets and liabilities of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities is the implied fair value of goodwill. The Group has one reporting unit and has determined to perform the annual impairment test on December 31 of each year. In 2012, the Group first assessed the qualitative factors to determine it is not more likely than not that the fair value of the reporting unit is less than its carrying amount. The Group did not incur any impairment loss on goodwill for the years ended December 31, 2010, 2011 or 2012.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(n) Revenue recognition*

The Group's revenues are principally derived from sales of products and services.

Specifically, sales of products include:

- (1) Sales of smart cards; and
- (2) Sales of other products.

Sales of services include the following four arrangements:

- (1) Head-end software, hardware and related system integration service ( SI service );
- (2) Head-end system development service ( SD service );
- (3) Licensing income; and
- (4) Royalty income.

*Sales of smart cards*

Smart cards are manufactured by third-party manufacturers based on the Group's blueprints. When the Group receives these products from the manufacturers, the Group programs each one with a unique security code so that it can communicate with the Group's CA systems. Revenue is recognized after a sales agreement is signed, the price is fixed or determinable, products are delivered to customers, and collection of the resulting receivables is assured. The Group also offers some of its customers a lower price or a certain amount of free cards when the cumulative volume of smart card purchases from the same customer is greater than a set volume during a specific period. The Group accounts for cumulative volume customer incentives as deferred revenue which is deducted against the initial revenue.

The Group generally guarantees the quality of smart cards for periods ranging from one to three years, and if any smart cards are found defective during the warranty period, the Group is obligated to replace them at the Group's cost. Historically, the defect rate of smart cards has been low and the Group accrues warranty liabilities based on historical information.

*Sales of others products*

The Group also derives revenues from the sales of products other than smart cards, such as integrated chips and other products. Revenue is recognized after a sales agreement is signed, the price is fixed or determinable, products are delivered to customers, and collection of the resulting receivables is assured.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(n) Revenue recognition* continued

*SI service*

For the SI service, the Group signs contracts with cable network operators to install and integrate the Group's software with the hardware and software purchased from third-party suppliers. The Group's software includes CA systems software, subscriber management system software and head-end electronic program guide software.

CA systems software consists of software that is installed at the premises of the television network operator, or the head end. CA systems enable television network operators to deliver secured contents and services to their subscribers.

Subscriber management system is software used by television network operators to support their operation, archive subscriber information and operational information, and to generate billings to subscribers.

Head-end electronic program guide software is software that enables television network operators to distribute Digital Video Broadcasting standard program specific information and service information to the subscribers.

Deliverables of SI service include: software, hardware, integration, installation, training and post-contract customer support ( PCS ). When the provision of services is substantially completed, i.e., when the Group delivers its software, purchases the hardware and software from third-party suppliers, integrates them together, and provides installation and training to customers, customers sign the preliminary acceptance. Final acceptance is typically signed six months to one year after the issuance of the preliminary acceptance if no major technical problems are discovered. Software is considered delivered to customers when preliminary acceptance is signed because only at that time customers are able to use the software in the integrated system. For majority of the contracts, the Group offers one-year free PCS, including telephone support and bug-fixing beginning from preliminary acceptance. However, in some of the contracts, the Group offers free PCS for a period of more than one year beginning from preliminary acceptance; while in some other contracts, the PCS does not have a specified definite period.

The SI service includes a significant software portion. The software is not regarded as incidental to the provision of services as a whole because the marketing of such services focuses on the internally developed technologies included in the software. Revenue is recognized when the last deliverable in the arrangement is delivered and when all of the following criteria have been met:

- (1) Persuasive evidence of an arrangement exists;
- (2) Delivery has occurred;
- (3) The vendor's fee is fixed or determinable; and
- (4) Collectability is probable.

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**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(n) Revenue recognition* continued

*SI service* continued

The systems are installed and tested at the customers' sites. Generally all the technical issues are identified and resolved before the preliminary acceptance is signed by the customers. Afterwards, the customers will begin to use the installed systems for operation.

For the contracts where the Group offers free PCS for one year or less, the cost incurred between the preliminary acceptance and the end of the free PCS period has historically been insignificant. Therefore, revenue is recognized when the entire installation and integration of software is completed, which is indicated by obtaining the preliminary acceptance from customers. For contracts where the Group offers free PCS for more than one year, the Group defers the revenue for the contracts and recognizes it over the PCS term although the cost incurred during the PCS term has been historically insignificant. Where the PCS term has no specified definite period, the Group recognizes such revenue over the estimated useful life of the CA systems, which the Group has determined to be five years.

*SD service*

The Group develops head-end system applications relating to digital TV technology for its customers.

Deliverables in SD service include the completed software application. A few arrangements also include one-year free PCS starting from customer acceptance, but no arrangement includes free PCS for more than one year. Payment terms vary based on the stage of the service. Normally a portion of the contract amount is paid when the contract is signed, and the remaining is paid upon the completion of the project and customer acceptance. The cost of providing free PCS has historically been insignificant.

Because a system development arrangement requires significant production, modification, or customization of software, the group refers to FASB Accounting Standards Codification (ASC) 605-35, *Construction-Type and Production-Type Contracts* for revenue recognition. As the Group cannot properly measure progress toward completion, the completed-contract method is used. Revenue for system development is recognized when the system development is finished and accepted by the customer.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(n) Revenue recognition* continued

*Licensing income*

The Group coordinates with network operators to produce set-top boxes compatible with the Group's CA systems. The Group enters into contracts with set-top box manufacturers selected by customers and provides these manufacturers with CA systems terminal-end software that is integrated in the set-top boxes and which permits the unscrambling of digital TV broadcasts that have been transmitted by TV network operators who use the Group's CA systems. The set-top box manufacturers pay the Group a one-time license fee, which includes a testing and certifying fee, for obtaining the blueprints and technologies in the form of software. According to the contracts, these manufacturers are required to provide a set-top box prototype to the Group in order to obtain a certificate from the Group which indicates the set-top box is compatible with the Group's CA systems and suitable for mass-production. The licenses to set-top box manufacturers are perpetual once provided. No PCS is offered in the licensing arrangement. Licensing income is recognized when all revenue recognition criteria have been met, which is indicated by the issuance of a certificate to the set-top box manufacturer by the Group.

All advances from customers and prepaid fees received from customers or set-top box manufacturers are initially recognized as deferred revenue and revenue is recognized when the above revenue recognition criteria are met.

*Royalty income*

The Group receives royalties on sales of CA systems terminal-end software.

Royalties are received either from set-top box manufacturers, or from television network operators depending on which party the Group enters the contracts with.

Royalty revenue is recognized when earned and collectability is reasonably assured.

For royalty income collected from set-top box manufacturers, royalty revenue is recognized upon the receipt of sales reports from set-top box manufacturers and when payment is received.

For royalty income received from television network operators, the Group requests the television network operators to pay the royalty to the Group directly when they purchase the Group's smart cards, in which case all the revenue is recognized as part of the smart card sales when these smart cards are delivered to the customers.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

**(o) *Deferred costs***

Deferred costs are recognized mainly for cost incurred, which consist of hardware and software purchased from third-party suppliers directly associated with revenue from SI service contracts that provide free PCS for more than one year.

Deferred costs from SI service are recoverable through the future revenue streams and are recorded as an asset and amortized to cost of revenue over the same period that the revenue is recognized. Amortization of deferred costs for the years ended December 31, 2010, 2011 and 2012 totaled \$401, \$535 and \$688, respectively.

**(p) *Value added tax ( VAT ) and VAT refund***

VAT on sales is calculated at 17% on revenue from product sales and SI Services and paid after deducting input VAT on purchases. The net VAT balance between input VAT and output VAT is reflected in the accounts under other taxes payable.

For certain software related products that are qualified as software products by PRC tax authorities, the Group can pay VAT at 17% first and then receive 14% refund after it is paid. The Group records VAT refund receivables on accrual basis. VAT refund is recorded in revenue in the statements of operations.

In July 2012, the Ministry of Finance and the State Administration of Taxation jointly issued Circular No. 71 regarding the pilot collection of VAT in lieu of business tax in certain areas and industries in the PRC. Starting from September 1, 2012, certain subsidiaries and VIE became subject to VAT at the rates of 6% on certain service revenues such as royalty income which were previously subject to business tax.

**(q) *Business tax***

The Group's PRC subsidiaries, VIE and VIE's subsidiaries are subject to business taxes, surcharges or cultural business construction fees on revenues related to certain types of services, and the net revenues are presented net of those taxes and fees incurred.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

**(r) Government subsidies**

Government subsidies mainly represent amounts granted by local government authorities as an incentive for companies to promote development of the local technology industry. When the Group receives the subsidies related to government sponsored projects, the subsidies are recorded as a liability and are recognized as subsidy income when there is no further performance obligation. Subsidy income of \$89, \$168 and \$351 were recognized for the years ended December 31, 2010, 2011 and 2012, respectively.

**(s) Operating leases**

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Payments made under operating leases are charged to the consolidated statements of operations on a straight-line basis over the lease periods.

**(t) Foreign currency translation**

The functional and reporting currency of the Company and the Company's subsidiaries outside the PRC is US dollar. The functional currency of the Company's subsidiaries, VIE and VIE's subsidiaries in the PRC is Renminbi ( RMB ).

Monetary assets and liabilities denominated in currencies other than the applicable functional currencies are translated into the functional currencies at the prevailing rates of exchange at the balance sheet date. Nonmonetary assets and liabilities are remeasured into the applicable functional currencies at historical exchange rates. Transactions in currencies other than the applicable functional currencies during the year are converted into the functional currencies at the applicable rates of exchange prevailing at the transaction dates. Transaction gains and losses are recognized in the consolidated statements of operations.

For translating the results of the PRC subsidiaries into the reporting currency of the Company, assets and liabilities are translated from each subsidiary's functional currency to the reporting currency at the exchange rate on the balance sheet date. Equity amounts are translated at historical exchange rates, and revenues, expenses, gains and losses are translated using the average rate for the period. Translation adjustments are reported as cumulative translation adjustments and are shown as a separate component of other comprehensive income in the consolidated statements of comprehensive income.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

***(u) Income taxes***

Deferred income taxes are provided using the asset and liability method. Under this method, deferred income taxes are recognized based on net operating losses available for carry-forwards and significant temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis using enacted tax rates in effect for the year in which the differences are expected to reverse. 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. A valuation allowance is provided to reduce the amount of deferred tax assets if it is considered more likely than not that some portion of, or all of the deferred tax assets will not be realized. Income taxes are provided for in accordance with the laws and regulations applicable to the Group as enacted by the relevant tax authorities. 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 of the related tax authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained.

***(v) Comprehensive income***

Comprehensive income includes net income and foreign currency translation adjustments. The consolidated financial statements have been adjusted for the retrospective application of the authoritative guidance regarding presentation of comprehensive income, which was adopted by the Company on January 1, 2012.

***(w) Net income per share***

Basic earnings per ordinary share is computed by dividing net income attributable to ordinary shareholders by weighted average number of ordinary shares outstanding during the period.

Diluted earnings per ordinary share reflects the potential dilution that could occur if securities were exercised or converted into ordinary shares. The Group had stock options which could potentially dilute basic earnings per share in the future. To calculate the number of shares for diluted income per share, the effect of the stock options is computed using the treasury stock method.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(x) Research and development expenses*

Research and development expenses are incurred in the development of the Group's products and technologies, including significant improvements and refinements to existing products and services. All research and development expenses are expensed as incurred.

*(y) Share-based compensation*

Share-based payment transactions with employees and directors, such as share options, are measured based on the grant date fair value of the equity instrument issued. Share-based compensation expenses, net of forfeitures, are recognized over the requisite service period based on the graded vesting attribution method, with a corresponding impact reflected in additional paid-in capital.

The Group recognizes the estimated compensation expenses of performance-based stock options based on the grant date fair value. The awards are earned upon attainment of identified performance goals. The Group recognizes the compensation expenses, net of estimated forfeitures, over the performance period. The Group also adjusts the compensation expenses based on the probability of performance goal achievement at the end of each reporting period.

Forfeitures are estimated at the time of grant and revised in the subsequent periods if actual forfeitures differ from those estimates. The Group uses historical data to estimate pre-vesting option forfeitures and record share-based compensation expenses only for those awards that are expected to vest.

A change in any of the terms or conditions of share options shall be accounted for as a modification of the plan. Therefore, the Group calculates incremental compensation cost of a modification as the excess of the fair value of the modified option over the fair value of the original option immediately before its terms are modified, measured based on the share price and other pertinent factors at the modification date. For vested options, the Group would recognize incremental compensation cost in the period of the modification occurred and for unvested options, the Group would recognize, over the remaining requisite service period, the sum of the incremental compensation cost and the remaining unrecognized compensation cost for the original award on the modification date.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(z) Fair value*

Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Group considers the principal or most advantageous market in which it would transact and it considers assumptions that market participants would use when pricing the asset or liability.

Fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The level in the hierarchy within which the fair value measurement in its entirety falls is based upon the lowest level of input that is significant to the fair value measurement as follows:

Level 1 inputs are based upon unadjusted quoted prices for identical assets or liabilities traded in active markets.

Level 2 inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques.

The Company measures certain assets, including the cost method investments and equity method investments, at fair value on a nonrecurring basis when they are deemed to be other-than-temporarily impaired. The fair values of these investments are determined based on valuation techniques using the best information available, and may include management judgments, future performance projections, etc. An impairment charge is recorded when the cost of the investment exceeds its fair value and this condition is determined to be other-than-temporary.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(aa) Recently issued accounting pronouncements*

In May 2011, the FASB issued an authoritative pronouncement on fair value measurement. The guidance is the result of joint efforts by the FASB and International Accounting Standards Board to develop a single, converged fair value framework. The guidance is largely consistent with existing fair value measurement principles in US GAAP. The guidance expands the existing disclosure requirements for fair value measurements and makes other amendments, mainly including:

Highest-and-best-use and valuation-premise concepts for nonfinancial assets-the guidance indicate that the highest-and-best-use and valuation-premise concepts only apply to measuring the fair value of nonfinancial assets.

Application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk-the guidance permits an exception to fair value measurement principles for financial assets and financial liabilities (and derivatives) with offsetting positions in market risks or counterparty credit risk when several criteria are met. When the criteria are met, an entity can measure the fair value of the net risk position.

Premiums or discounts in fair value measure-the guidance provides that premiums or discounts that reflect size as a characteristic of the reporting entity's holding (specifically, a blockage factor that adjusts the quoted price of an asset or a liability because the market's normal daily trading volume is not sufficient to absorb the quantity held by the entity) rather than as a characteristic of the asset or liability (for example, a control premium when measuring the fair value of a controlling interest) are not permitted in a fair value measurement.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(aa) Recently issued accounting pronouncements* continued

Fair value of an instrument classified in a reporting entity's stockholders' equity-the guidance prescribes a model for measuring the fair value of an instrument classified in stockholders' equity; this model is consistent with the guidance on measuring the fair value of liabilities.

Disclosures about fair value measurements-the guidance expands disclosure requirements, particularly for Level 3 inputs. Required disclosures include:

- (i) For fair value measurements categorized in Level 3 of the fair value hierarchy: (1) a quantitative disclosure of the unobservable inputs and assumptions used in the measurement, (2) a description of the valuation process in place (e.g., how the entity decides its valuation policies and procedures, as well as changes in its analyses of fair value measurements, from period to period), and (3) a narrative description of the sensitivity of the fair value to changes in unobservable inputs and interrelationships between those inputs.
- (ii) The level in the fair value hierarchy of items that are not measured at fair value in the statement of financial position but whose fair value must be disclosed.

The guidance is to be applied prospectively and is effective for interim and annual periods beginning after December 15, 2011, for public entities. Early application by public entities is not permitted. The Group adopted this pronouncement effectively January 1, 2012, which did not have a significant effect on the Company's consolidated financial statements.

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**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(aa) Recently issued accounting pronouncements continued*

In June 2011, the FASB issued an authoritative pronouncement to require an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The guidance does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The guidance should be applied retrospectively. For public entities, the guidance is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. In December 2011, the FASB issued an authoritative pronouncement related to deferral of the effective date for amendments to the presentation of reclassifications of items out of accumulated other comprehensive income. This guidance allows the FASB to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the FASB is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before update the pronouncement issued in June 2011. The Company adopted this guidance on January 1, 2012 and has presented a single continuous consolidated statements of comprehensive income since that date.

In September 2011, the FASB issued an authoritative pronouncement related to testing goodwill for impairment. The guidance is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. The guidance permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if a public entity's financial statements for the most recent annual or interim period have not yet been issued. The Group adopted this pronouncement effective January 1, 2012, which did not have a significant effect on the Company's consolidated financial statements.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(aa) Recently issued accounting pronouncements continued*

In December 2011, the FASB has 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 (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 Group does not expect the adoption of this pronouncement will have a significant impact on its financial condition or results of operations.

In July 2012, the FASB has issued an authoritative pronouncement related to testing indefinite-lived intangible assets, other than goodwill, for impairment. Under the pronouncement, entities testing indefinite-lived intangible assets for impairment would have the option of performing a qualitative assessment before calculating the fair value of the asset. If an entity determines, on the basis of qualitative factors, that the indefinite-lived intangible asset is not more likely than not impaired, a quantitative fair value calculation would not be needed. The amendments are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The Group does not expect the adoptions of this pronouncement will have a significant impact on its financial condition or results of operations.

In February 2013, the FASB has 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 amendments in this ASU do not change the current requirements for reporting net income or other comprehensive income in financial statements. All of the information that this ASU requires already is required to be disclosed elsewhere in the financial statements under U.S. GAAP.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(aa) Recently issued accounting pronouncements* continued

The new amendments 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 U.S. GAAP to be reclassified to net income in its entirety in the same reporting period.

Cross-reference to other disclosures currently required under U.S. GAAP for other reclassification items (that are not required under U.S. 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 amendments apply to all public and private companies that report items of other comprehensive income. Public companies are required to comply with these amendments for all reporting periods (interim and annual). The amendments are effective for reporting periods beginning after December 15, 2012, for public companies. Early adoption is permitted. The Group does not expect the adoption of this pronouncement will have a significant impact on its financial condition or results of operations.

In March 2013, the FASB has 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. The Group does not expect the adoption of this pronouncement will have a significant impact on its financial condition or results of operations.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued**

*(aa) Recently issued accounting pronouncements* continued

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 amendments in this pronouncement clarify 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 amendments in this pronouncement are effective prospectively for fiscal years (and interim reporting periods within those years) beginning after December 15, 2013. The amendments 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 amendments, it should apply them as of the beginning of the entity's fiscal year of adoption. The Group does not expect the adoption of this pronouncement will have a significant impact on its financial condition or results of operations.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****3. SEGMENT INFORMATION AND REVENUE ANALYSIS**

The Group's chief operating decision maker is the Chief Executive Officer, who reviews consolidated results of operations prepared in accordance with U.S. GAAP when making decisions about allocating resources and assessing performance of the Group. The Group has only one operating segment.

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

The gross revenues consist of the following products and services:

|                             | For the years ended December 31, |            |           |
|-----------------------------|----------------------------------|------------|-----------|
|                             | 2010                             | 2011       | 2012      |
| <b>Products:</b>            |                                  |            |           |
| Smart cards                 | \$ 82,153                        | \$ 91,960  | \$ 75,185 |
| Other products              | 365                              | 3,202      | 10,134    |
| Subtotal                    | 82,518                           | 95,162     | 85,319    |
| <b>Services:</b>            |                                  |            |           |
| Head-end system integration | 2,399                            | 2,562      | 2,175     |
| Head-end system development | 595                              | 736        | 987       |
| Licensing income            | 1,565                            | 1,328      | 1,246     |
| Royalty income              | 662                              | 742        | 382       |
| Other services              | 4                                | 10         | 135       |
| Subtotal                    | 5,225                            | 5,378      | 4,925     |
| Total                       | \$ 87,743                        | \$ 100,540 | \$ 90,244 |

VAT refunds of \$7,624, \$8,377, and \$7,366 were included in revenues for the years ended December 31, 2010, 2011 and 2012, respectively.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****4. ACQUISITION**

On February 26, 2010, the Group entered into an agreement with Beijing Shi Xun Hu Lian Technology Co, Ltd. ( Beijing Shi Xun ), a related party of the Group, to acquire its 90% equity interest in Guangdong R&D for a cash consideration of \$396. On the same day, the Group entered into an agreement with the holder of the remaining 10% equity interest in Guangdong R&D, an independent third party of the Group, for a cash consideration of \$44. Guangdong R&D is a china-based company with limited operation. The purpose of the acquisition is to use this company to conduct research and development in TV digitalization. These transactions were closed on February 28, 2010 and Guangdong R&D became a wholly owned subsidiary of the Group after March 2010.

The transaction was accounted for as a business combination using the acquisition method of accounting. The purchase price allocation of the transaction was allocated to assets acquired as of the date of acquisition as follows:

|                                  |        |
|----------------------------------|--------|
| Fair value of net asset acquired | \$ 440 |
| Total consideration              | \$ 440 |

No intangible assets and goodwill were recognized.

It is not practical without unreasonable efforts to present the supplemental unaudited pro form results of operations of the Group for the year ended December 31, 2010 assuming that the acquisition of Guangdong R&D had been completed on January 1, 2010.

**5. RESTRICTED CASH**

Restricted cash consists of the following:

|  | As of December 31, |       |
|--|--------------------|-------|
|  | 2011               | 2012  |
| Bank deposits pledged as security for issuing letters of credit  | \$ 210             | \$ 18 |
| Bank deposits pledged as security for short-term loans (Note 14) | 55,469             |       |
| Restricted cash  | \$ 55,679          | \$ 18 |

**6. NOTES RECEIVABLE**

Notes receivable represents bank acceptance drafts that are non-interest bearing and due within six months.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****7. ACCOUNTS RECEIVABLE, NET**

Accounts receivable, net, consists of the following:

|                                       | As of December 31, |           |
|---------------------------------------|--------------------|-----------|
|                                       | 2011               | 2012      |
| Accounts receivable                   | \$ 31,875          | \$ 40,506 |
| Less: allowance for doubtful accounts | (845)              | (2,223)   |
| Accounts receivable, net              | \$ 31,030          | \$ 38,283 |

Movement of allowance for doubtful accounts is as follows:

|      | Balance at<br>beginning<br>of the year | Charge to<br>expenses | Deductions | Balance at<br>end of the<br>year |
|------|--|-----------------------|------------|----------------------------------|
| 2011 | \$ 758                                 | \$ 87                 | \$         | \$ 845                           |
| 2012 | \$ 845                                 | \$ 1,378              | \$         | \$ 2,223                         |

**8. INVENTORIES**

Inventories, net consist of the following:

|                  | As of December 31, |          |
|------------------|--------------------|----------|
|                  | 2011               | 2012     |
| Raw materials    | \$ 2,036           | \$ 1,134 |
| Finished goods   | 1,882              | 4,544    |
| Inventories, net | \$ 3,918           | \$ 5,678 |

Movement of provision for inventory was as follows:

|                                  | December 31, |        |        |
|----------------------------------|--------------|--------|--------|
|                                  | 2010         | 2011   | 2012   |
| Balance at beginning of the year | \$ 370       | \$ 405 | \$ 450 |
| Charge to expenses               | 35           | 45     | 217    |

|                            |        |        |        |
|----------------------------|--------|--------|--------|
| Balance at end of the year | \$ 405 | \$ 450 | \$ 667 |
|----------------------------|--------|--------|--------|

F-39

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****9. PREPAID EXPENSES AND OTHER CURRENT ASSETS**

Prepaid expenses and other current assets consist of the following:

|  | As of December 31, |          |
|--|--------------------|----------|
|  | 2011               | 2012     |
| Interest receivables                           | \$ 1,619           | \$ 241   |
| Receivable from disposal of Dongguan Super TV* | 1,046              |          |
| Deposits                                       | 654                | 638      |
| VAT refund receivables                         | 920                | 2,766    |
| Prepayments to suppliers                       | 979                | 1,176    |
| Fair value of the Forward Contracts (Note 14)  | 404                |          |
| Other prepaid expenses                         | 1,146              | 424      |
|  | \$ 6,768           | \$ 5,245 |

\* In December 2011, the Group entered into an agreement with a third party to sell all of its equity interest in Dongguan Super TV with consideration of \$1,046, which was received in the year ended December 31, 2012.

**10. PROPERTY AND EQUIPMENT, NET**

Property and equipment, net, consist of the following:

|   | As of December 31, |          |
|---|--------------------|----------|
|   | 2011               | 2012     |
| Computers and other electronic equipment        | \$ 4,048           | \$ 3,905 |
| Furniture and fixtures                          | 184                | 208      |
| Leasehold improvements                          | 1,241              | 1,055    |
| Motor vehicles                                  | 587                | 594      |
|   | 6,060              | 5,762    |
| Less: accumulated depreciation and amortization | (4,309)            | (4,132)  |
|   | \$ 1,751           | \$ 1,630 |

For the years ended December 31, 2010, 2011 and 2012, depreciation expense was \$1,005, \$1,092 and \$921, respectively.



**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****11. INTANGIBLE ASSETS, NET**

Intangible assets, net, consist of the following:

|   | As of December 31, |         |
|---|--------------------|---------|
|   | 2011               | 2012    |
| Core technology                                   | \$ 477             | \$ 482  |
| Complete technology                               | 73                 | 73      |
| Contract backlogs                                 | 336                | 336     |
| Customer relationship                             | 1,188              | 1,188   |
| Digital watermarking technology                   | 952                | 962     |
| Image tracing technology                          | 410                | 410     |
|   | 3,436              | 3,451   |
| Less: accumulated amortization                    |                    |         |
| Core technology                                   | (322)              | (385)   |
| Complete technology                               | (73)               | (73)    |
| Contract backlogs                                 | (336)              | (336)   |
| Customer relationship                             | (1,188)            | (1,188) |
| Digital watermarking technology                   | (603)              | (793)   |
| Image tracing technology                          | (119)              | (119)   |
|   | (2,641)            | (2,894) |
| Less: impairment loss of image tracing technology | (291)              | (291)   |
| Foreign exchange difference                       | (54)               | (68)    |
|   | \$ 450             | \$ 198  |

Intangible assets related to complete technology, contract backlogs and customer relationship have been fully amortized as of December 31, 2012. Image tracing technology has been amortized and impaired to zero as of December 31, 2010.

The Group recorded amortization expense of \$267, \$251 and \$253 for the years ended December 31, 2010, 2011 and 2012, respectively. Estimated amortization expenses of the existing intangible assets for the next five years are \$192, \$6, nil, nil and nil respectively.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****12. EQUITY METHOD INVESTMENTS**

Equity method investments consist of the following:

|  | Notes | As of December 31, |          |
|--|-------|--------------------|----------|
|  |       | 2011               | 2012     |
| Nanjing Qingda Yongxin Culture Media Co., Ltd. ( Qingda Yongxin )      | (a)   | \$ 67              | \$ 67    |
| Foshan Nanhai Guokai Digital TV Technology Co., Ltd. ( Nanhai Guokai ) | (b)   | 348                | 358      |
| 3DiJoy Corp. ( 3DiJoy )  | (c)   | 5,065              |          |
| Guangzhou Rujia Network Technology Co., Ltd., ( Rujia )                | (d)   | 2,286              | 2,591    |
| Beijing Shibo Movie Technology Co., Ltd. ( Shibo Movie )               | (e)   |                    | 648      |
| Beijing Xinghe Union Media Co., Ltd. ( Xinghe Union )                  | (f)   |                    | 604      |
|  |       | \$ 7,766           | \$ 4,268 |

- (a) In March 2007, the Group and Jiangsu Qingda Technology Co. Limited ( Jiangsu Qingda ), one of its customers, set up a joint venture Qingda Yongxin, in which the Group contributed cash of \$103, representing 40% of equity interest in the joint venture. Jiangsu Qingda contributed cash of \$155 representing 60% of equity interest in the joint venture.

The Group has accounted for this long-term investment using equity method of accounting because the Group does not control the investee but has the ability to exercise significant influence over the operating and financial policies of the investee.

- (b) In July 2007, the Group acquired 51% equity interest in Nanhai Guokai from N-T Information Engineering at the cash consideration of \$296. Nanhai Guokai is a company primarily engaged in research, development and sales of digital TV-related systems, software and products. A Japanese multinational company holds the remaining 49% equity interest in Nanhai Guokai.

The Group has accounted for this long-term investment using equity method of accounting because the Group does not control the investee but has the ability to exercise significant influence over operating and financial policies of the investee. The Group controls three out of five seats in the board of directors of Nanhai Guokai. The remaining two seats are controlled by the other shareholder. According to the article of association of Nanhai Guokai, two-thirds of directors' approval is required for the appointment and dismissal of the general manager and vice general manager. Therefore the other shareholder has substantive rights to participate in significant operating decisions in Nanhai Guokai. Accordingly, the Group accounts for its investment in Nanhai Guokai using the equity method of accounting.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**12. EQUITY METHOD INVESTMENTS continued**

- (c) In May 2010, the Group entered into a share subscription agreement to purchase 24% of equity interest in 3DiJoy with a consideration of \$6,000. The Group had accounted for this long-term investment using equity method of accounting because the Group does not control the investee but has the ability to exercise significant influence over the operating and financial policies of the investee. 3DiJoy has been experiencing financial difficulties in 2012 while it was actively searching for the new capital injection for its operation. In the third quarter of 2012, 3DiJoy assessed that there was no alternative investment and due to the absence of further shareholders' support, it did not expect to operate as a going concern and it laid off nearly half of the employees. As such, as of September 30, 2012 the Company performed the impairment analysis with the assistance of a third party valuer on the investment. The fair value of 3DiJoy decreased significantly below its carrying value and the decrease was other-than temporary. As a result, the Company did not expect to receive any return from this investment and concluded that a full impairment of \$4,487 was recognized in 2012.
- (d) In June 2010, the Group acquired 34.45% of equity interest in Rujia through purchase of existing shares from a shareholder of Rujia and contribution to its capital increase, for a total consideration of \$2,500. The Group has accounted for this long-term investment using equity method of accounting because the Group does not control the investee but has the ability to exercise significant influence over the operating and financial policies of the investee.
- (e) In February 2012, the Group and Beijing AirMedia Advertising Co., Ltd., set up a joint venture Shibo Movie, in which the group contributed cash of \$794, representing 50% of equity interest in joint venture. The Group has accounted for this long-term investment using equity method of accounting because the Group does not control the investee but has the ability to exercise significant influence over the operating and financial policies of the investee.
- (f) In March 2012, the Group and Beijing AirMedia Advertising Co., Ltd., set up a joint venture Xinghe Union, in which the group contributed cash of \$794, representing 50% of equity interest in joint venture. The Group has accounted for this long-term investment using equity method of accounting because the Group does not control the investee but has the ability to exercise significant influence over the operating and financial policies of the investee.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****12. EQUITY METHOD INVESTMENTS continued**

The combined financial information for the equity method investments as of and for the periods presented is as follows:

|                           | As of December 31, |          |
|---------------------------|--------------------|----------|
|                           | 2011               | 2012     |
| Total current assets      | \$ 7,711           | \$ 9,434 |
| Total assets              | 8,614              | 10,111   |
| Total current liabilities | 1,032              | 2,040    |
| Total liabilities         | \$ 1,196           | \$ 2,063 |

  

|                               | For the years ended December 31, |            |            |
|-------------------------------|----------------------------------|------------|------------|
|                               | 2010                             | 2011       | 2012       |
| Total net revenue             | \$ 2,791                         | \$ 1,628   | \$ 3,847   |
| Income/(loss) from operations | \$ 99                            | \$ (3,310) | \$ (1,750) |

**13. COST METHOD INVESTMENTS**

On January 4, 2010, the Group, together with several other third parties entered into a share purchase agreement with OpenV China Holdings Company ( OpenV ) for a strategic investment in OpenV with equity interest of 11.5% (subject to adjustment based on OpenV's performance) for a consideration of \$5,000. The Group accounted for this long-term investment under the cost method of accounting because the Group does not have significant influence and a controlling interest over OpenV.

In October 2010, the Group was informed that OpenV was under investigation over alleged copyright infringements relating to some of its online video content. Its normal online video services had been suspended. Based on the foregoing, the Group has doubts on the going concern of OpenV. As a result, the Group wrote off the entire amount of original \$5,000 investment in OpenV.

In October 2012, the Group entered into a share redemption agreement with OpenV. Pursuant to the agreement, OpenV repurchased 460,080 of its shares for a consideration of \$820, which was recorded in other income in 2012. Considering the equity changes of OpenV, the Group holds 10.71% equity interest in Open V after the share repurchase as of December 31, 2012.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****14. FORWARD CONTRACTS**

To facilitate the cash payment of special cash dividend that the Group declared in November 2010, the Group entered into foreign currency forward contracts with two banks in April and May 2011. Pursuant to those contracts, the Group made short-term loan in US dollar from these two banks with an aggregated amount of \$55,193 for a period of one year. Meanwhile, the amount of \$55,469 of the Group's bank deposit was restricted until the short-term loan was fully paid back in April and May 2012 (Note 5). The forward contracts were determined to be a derivative. The Group carries the forward contracts at fair value in its balance sheet and the changes in the forward contract fair value during each period end are recorded in the statement of operations. The Group carries the forward contract as either assets or liabilities at fair value.

The Group measures the fair value of the forward contract on a recurring basis based on a level 2 measure, i.e. the Group uses the market forward exchange rate to assess the fair value of the forward contract and recognizes the changes in fair value attributable to the difference between the market forward exchange rate and contractual exchange rate in change in fair value of forward contract. For the year ended December 31, 2011 and 2012, the Group recorded a gain of \$404 and a loss of \$690 in change in fair value of forward contract respectively. The short-term loan and the forward contracts were settled in May 2012.

**15. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES**

Accrued expenses and other current liabilities consist of the following:

|                              | As of December 31, |           |
|------------------------------|--------------------|-----------|
|                              | 2011               | 2012      |
| Accrued payroll and bonus    | \$ 3,662           | \$ 3,753  |
| Other taxes payable          | 1,570              | 1,964     |
| Social insurance withholding | 475                | 695       |
| Provision for warranty       | 230                | 250       |
| Others                       | 3,376              | 5,643     |
|                              | \$ 9,313           | \$ 12,305 |

Movement of provision for warranty is as follows:

|      | Balance at<br>beginning<br>of the<br>year | Charge to<br>expenses | Deductions | Balance at<br>end of the<br>year |
|------|---|-----------------------|------------|----------------------------------|
| 2011 | \$ 183                                    | \$ 84                 | \$ (37)    | \$ 230                           |
| 2012 | \$ 230                                    | \$ 69                 | \$ (49)    | \$ 250                           |

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****16. DEFERRED REVENUE**

Deferred revenue consists of the following:

|   | As of December 31, |                 |
|---|--------------------|-----------------|
|   | 2011               | 2012            |
| <b>Current:</b>   |                    |                 |
| Advance from customers  | \$ 5,028           | \$ 6,179        |
| Incentive offered to customers  | 1,727              | 790             |
| Deferred revenue for SI service contracts with remaining PCS period within one year       | 990                | 504             |
|   | 7,745              | 7,473           |
| <b>Non-current:</b>   |                    |                 |
| Deferred revenue for SI service contracts with remaining PCS period greater than one year | 401                | 255             |
| <b>Total</b>  | <b>\$ 8,146</b>    | <b>\$ 7,728</b> |

Incentive offered to customers represents the deferred revenue relating to free smart cards committed to customers when cumulative purchase volume from the same customers reached certain level. Such deferred revenue is deducted from the initial revenue and to be recognized as revenue when free cards are delivered.

**17. INCOME TAXES**

CDTV Holdings and CDTV BVI are tax-exempted companies incorporated in the Cayman Islands and the British Virgin Islands, respectively.

Golden Benefit and CSM Holdings are subject to Hong Kong Profits Tax on its activities conducted in Hong Kong. No provision for Hong Kong Profits tax has been made in the consolidated financial statements as they both have no assessable profits for the years presented.

Super TV, N-S Digital TV, N-S Media Investment, Guangdong R&D, N-S Investment Holdings, Joysee, Cyber Cloud and Super Movie were registered in the PRC and are subject to PRC Enterprise Income Tax ( EIT ) on the taxable income in accordance with the relevant PRC income tax laws.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****17. INCOME TAXES continued**

Both Super TV and N-S Digital TV were qualified as New and High-Tech Enterprise ( NHTE ) under the Enterprise Income Tax Law effective from January 1, 2008 (the 2008 EIT law ) and therefore both of them were qualified for a preferential tax rate of 15% for a three year period. In October 2011, Super TV and N-S Digital TV renewed for NHTE qualification and both entities were entitled to a preferential tax rate of 15% for a further three year period.

Super TV was qualified as Key Software Enterprise in 2010 under the 2008 EIT law and entitled for a preferential tax rate of 10% in 2010. As of December 31, 2012, the application to renew the status for the year of 2011 and 2012 has not been approved. Therefore, Super TV applied tax rate of 15%. In March 2013, Super TV obtained the Key Software Enterprise certificate for the tax years from 2011 to 2012 from the relevant PRC government authorities and, as a result, was entitled to a preferential income tax rate of 10% in each of those years.

N-S Media Investment, N-S Investment Holdings and Guangdong R&D were subject to the statutory tax rate of 25% in 2010, 2011, and 2012.

Joysee, Cyber Cloud and Super Movie, established in 2011, were subject to the statutory tax rate of 25% in 2011 and 2012.

Deferred income taxes result principally from differences in the recognition of certain assets and liabilities for tax and financial reporting purposes and the tax effect of tax loss carry forwards.

Income tax expenses/(benefits) are as follows:

|                                | For the years ended December 31, |           |           |
|--------------------------------|----------------------------------|-----------|-----------|
|                                | 2010                             | 2011      | 2012      |
| Income tax expenses/(benefits) |                                  |           |           |
| Current                        | \$ 10,714                        | \$ 10,344 | \$ 18,035 |
| Deferred                       | (464)                            | (582)     | 4,197     |
| Total                          | \$ 10,250                        | \$ 9,762  | \$ 22,232 |

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****17. INCOME TAXES continued**

The principal components of the deferred income tax assets (liabilities) are as follows:

|   | As of December 31, |                   |
|---|--------------------|-------------------|
|   | 2011               | 2012              |
| <b>Current deferred tax assets</b>                                  |                    |                   |
| Write-down of inventory value                                       | \$ 64              | \$ 110            |
| Allowance for doubtful accounts                                     | 127                | 356               |
| Accrued expenses  | 471                | 604               |
| Accrued bonus   | 476                | 439               |
| Deferred revenue-current  | 394                | 176               |
| Deferred cost-current   | (44)               | 3                 |
| Warranty  | 35                 | 37                |
| Valuation allowance   | (171)              | (222)             |
| <b>Current deferred tax assets subtotal</b>                         | <b>1,352</b>       | <b>1,503</b>      |
| <b>Non-current deferred tax assets</b>                              |                    |                   |
| Deferred revenue-non-current  | 120                | 172               |
| Government subsidies  | 271                | 616               |
| Intangible assets amortization                                      | 73                 | 65                |
| Intangible assets impairment  | 47                 | 48                |
| Deferred cost-non-current   | (56)               | (14)              |
| Tax loss carry-forward deferred tax assets                          | 3,161              | 4,675             |
| Valuation allowance   | (3,161)            | (4,765)           |
| <b>Non-current deferred tax assets subtotal</b>                     | <b>\$ 455</b>      | <b>\$ 797</b>     |
| <b>Non-current deferred tax liabilities</b> Accrued withholding tax |                    | <b>(4,812)</b>    |
| <b>Non-current deferred tax liabilities subtotal</b>                | <b>\$</b>          | <b>\$ (4,812)</b> |

The Group's subsidiaries registered in the PRC have total net operating loss carry forwards of \$18,700 as of December 31, 2012 which will expire on various dates between December 31, 2013 and December 31, 2017. The net operating loss carry forwards generated by a particular entity in the Group cannot be transferred or utilized by other entities within the Group. Valuation allowances have been established because the Group believes that it is more likely than not that its deferred tax assets will not be realized as it does not expect to generate sufficient taxable income in future.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****17. INCOME TAXES continued**

Reconciliation between the provision for income taxes computed by applying the PRC EIT rates of 25% to income before income taxes and the actual provision of income taxes is as follows:

|   | For the years ended December 31, |           |           |
|---|----------------------------------|-----------|-----------|
|   | 2010                             | 2011      | 2012      |
| Net income before provision for income taxes                | \$ 43,812                        | \$ 51,084 | \$ 28,410 |
| PRC statutory tax rate                                      | 25%                              | 25%       | 25%       |
| Income tax at statutory tax rate                            | 10,953                           | 12,771    | 7,103     |
| Expenses not deductible for tax purposes                    | 194                              | 230       | 550       |
| Effect of income tax exemptions                             | (8,829)                          | (6,567)   | (4,470)   |
| Effect of income tax rate difference in other jurisdictions | 1,627                            | 1,901     | 1,916     |
| Change in valuation allowance                               | 925                              | 1,427     | 1,655     |
| Withholding tax   | 5,380                            |           | 14,296    |
| Expense adjustment related to non-taxable income*           |                                  |           | 1,182     |
| Income tax expenses   | \$ 10,250                        | \$ 9,762  | \$ 22,232 |

\* The adjustment is related to non-deductible expenditure incurred in connection to income claimed for VAT refund for prior periods.

If N-S Digital TV and Super TV were not in a tax holiday period for the years ended December 31, 2010, 2011 and 2012, the impact to the earnings per share amounts would be as follows:

|  | For the years ended December 31, |          |          |
|--|----------------------------------|----------|----------|
|  | 2010                             | 2011     | 2012     |
| Increase in income tax expense           | \$ 8,829                         | \$ 6,567 | \$ 4,470 |
| Decrease in net income per share-basic   | 0.15                             | 0.11     | 0.08     |
| Decrease in net income per share-diluted | \$ 0.15                          | \$ 0.11  | \$ 0.08  |

Uncertainties exist with respect to how the current income tax law in the PRC applies to the Group's overall operations, and more specifically, with regard to tax residency status. The 2008 EIT Law includes a provision specifying that legal entities organized outside the PRC will be considered residents for Chinese income tax purposes if the place of effective management or control is within the PRC. The implementation rules to the New EIT Law provide that non-resident legal entities will be considered PRC residents if substantial and overall management and control over the manufacturing and business operations, personnel, accounting, properties, etc., occurs within the PRC. Despite the present uncertainties resulting from the limited PRC tax guidance on the issue, the Group does not believe that the legal entities organized outside the PRC should be treated as residents for 2008 EIT law purposes. If the PRC tax authorities subsequently determine that the Company and its subsidiaries registered outside the PRC should be deemed resident enterprises, the Company and its subsidiaries registered outside the PRC will

be subject to the PRC income tax at a rate of 25%.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**17. INCOME TAXES continued**

If the Company were to be non-resident for PRC tax purpose, dividends paid to it from profits earned by the PRC subsidiary after January 1, 2008 would be subject to a withholding tax. In the case of dividends paid by PRC subsidiaries, the withholding tax would be 10% and in the case of a subsidiary 25% or more directly owned by the resident in Hong Kong, the withholding tax would be 5%, but that will be subject to the interpretation of Circular No. 601 issued by the State Administration of Taxation, under which the Company's Hong Kong subsidiary might not be considered to be the beneficial owner of any such dividends and in that case the withholding tax rate would be 10%.

Under the applicable accounting principles, a deferred tax liability should be recorded for taxable temporary differences attributable to the excess of financial reporting over tax basis, including those differences attributable to an investment in a subsidiary. However, recognition is not required in situations where the tax law provides means by which reported amount of that investment in subsidiary can be recovered tax-free and the enterprise expects that it will ultimately use that means.

In November 2012, Super TV distributed its earnings generated in 2010 and 2011 of \$92,779 dividend to its immediate foreign holding company, Golden Benefit, for purpose of special cash dividend distribution to shareholders of the Company. According to the interpretation of Circular No. 601 issued by the State Administration of Taxation, the Company's Hong Kong subsidiary might not be considered to be the beneficial owner of any such dividends and in that case the withholding tax rate would be 10%. As a result, withholding tax of \$9,278 was imposed.

Before the year 2012, the Company determined that the undistributed earnings of the Company's subsidiaries located in the PRC would be indefinitely reinvested for use in the operation and expansion of its business within PRC and no deferred tax liability had been accrued for the PRC dividend withholding tax for the undistributed retained earnings. In 2012, the Company determines to distribute the undistributed retained earnings of the Company's subsidiary located in the PRC without a set schedule. As a result, the Company accrued deferred tax liabilities related to withholding tax in the amount of \$4,812 on the undistributed earnings generated after January 1, 2008.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****18. NET INCOME PER SHARE**

|  | For the years ended December 31, |            |            |
|--|----------------------------------|------------|------------|
|  | 2010                             | 2011       | 2012       |
| Net income (numerator), basic and diluted  | \$ 33,421                        | \$ 41,000  | \$ 6,927   |
| Shares (denominator):  |                                  |            |            |
| Weighted average ordinary shares outstanding used in computing basic net income (loss) per share                         | 58,313,467                       | 58,934,912 | 59,011,396 |
| Effect of dilutive securities:   |                                  |            |            |
| Plus incremental weighted average ordinary shares from assumed exercise of stock options using the treasury stock method | 465,560                          | 140,554    | 81,408     |
| Total Weighted average ordinary shares outstanding used in computing diluted net income per ordinary share               | 58,779,027                       | 59,075,466 | 59,092,804 |
| Net income per share-basic   | \$ 0.57                          | \$ 0.70    | \$ 0.12    |
| Net income per share-diluted   | \$ 0.57                          | \$ 0.69    | \$ 0.12    |

The Company had 1,387,548, 4,237,890 and 644,790 stock options outstanding in 2010, 2011 and 2012, respectively, which could potentially dilute net income per share in the future, but were excluded in the computation of diluted net income per share in those periods, as their exercise prices were above the average market values in such periods.

**19. SPECIAL CASH DIVIDEND TO SHAREHOLDERS**

In November 2010, the Group declared a special cash dividend of \$2.00 per share on the Company's ordinary shares to be paid in two installments of \$1.00 each. The dividend was fully paid by May 31, 2011.

In May 2011, the Group declared a special cash dividend of \$0.56 per share on the Company's ordinary shares. The dividend was fully paid by the end of April 2012.

In November 2012, the Group declared a special cash dividend of \$2.3 per share on the Company's ordinary shares to be paid in two installments with total amount of \$135,933. \$59,013 was paid in 2012 and \$76,847 was paid in 2013. There was \$73 remaining unpaid as of April 16, 2013.

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**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION**

*(a) Option granted by the company*

*Option granted to employees*

Pursuant to the directors' resolution, the Group adopted Share Incentive Plans in 2005, under which the Group may grant options to purchase up to 4,444,440 ordinary shares of the Group, to its employees, directors, and consultants, subject to vesting requirements. Under Share Incentive Plans in 2005, there are four schemes of the options granted: Scheme I, Scheme II, Scheme III and Scheme IV, which were granted on February 3, 2005, September 22, 2006, December 5, 2006 and October 5, 2008, respectively. There were no share options granted under Scheme I and Scheme IV outstanding as of December 31, 2012.

On September 13, 2007, the board of directors of CDTV Holding approved the 2008 Stock Incentive Plan, pursuant to which the Group may grant options to purchase up to 1,200,000 ordinary shares to its employees and other eligible people. Under Share Incentive Plans in 2008, there are four schemes of the options granted: Scheme V, Scheme VI, Scheme VII and Scheme VIII, which were granted on October 5, 2008, June 2, 2009, February 10, 2010 and November 15, 2010, respectively. There were no share options granted under Scheme VII outstanding as of December 31, 2012.

On November 19, 2010, the board of directors of CDTV Holding approved the 2010 Stock Incentive Plan, pursuant to which the Group may grant options to purchase up to 3,600,000 ordinary shares to its employees and other eligible people. Scheme IX, Scheme X, Scheme XI and Scheme XII, which were granted on November 19, 2010, May 16, 2011, September 30, 2011 and November 19, 2011, respectively.

On May 1, 2012, the board of directors of CDTV Holding approved the 2012 Stock Incentive Plan, pursuant to which the Group may grant options to purchase up to 1,200,000 ordinary shares to its employees. As of December 31, 2012, no options were granted under the 2012 Stock Incentive Plan.

*Modification of option plans*

On November 19, 2010, the board of directors of CDTV Holding approved the exercise price of all options which are granted under the 2005 Plan, the 2008 Plan and the 2010 Plan prior to December 23, 2010 (the Adjusted Options) and remain outstanding as of December 23, 2010 shall be adjusted as follows to reflect the declaration and payment of the special cash dividend.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(a) Option granted by the company continued**

***Modification of option plans* continued**

The per share exercise price of all Adjusted Options with a per share exercise price higher than \$2.00 shall be reduced by \$2.00 on December 23, 2010; the per share exercise price of all Adjusted Options with a per share exercise price no more than \$2.00 shall be reduced to \$0.01. The modification to the share exercise price did not have any incremental compensation cost. The board also determined that if any future dividend is declared by the Board of the Company on all Ordinary Shares of the Company, the per share exercise price of all options granted prior to and outstanding as of the date of record of such dividend shall be reduced by an amount equal to the dividend payable on each Ordinary Shares, provided that the per share exercise price after adjustment shall not be less than \$0.01.

On May 20, 2011, as the Company declared a special cash dividend of \$0.56 per share on the Company's ordinary shares, the per share exercise price of all options granted prior to and remaining outstanding as of June 20, 2011, the record date, was reduced by \$0.56, provided that the per share exercise price after adjustment shall not be less than \$0.01.

On November 12, 2012, as the Company declared a special cash dividend of \$2.3 per share on the Company's ordinary shares, the per share exercise price of all options granted prior to and remaining outstanding as of November 26, 2012, the record date, was reduced by \$2.3, provided that the per share exercise price after adjustment shall not be less than \$0.01.

***Details of the Share Incentive Plans:***

***Scheme II***

Grant date: September 22, 2006

Exercise price per share original: \$1.771

Exercise price per share after modification: \$0.01

Expiration date: September 21, 2016

Number of options granted: 543,674

Vesting schedule: The option shall become vested as to (1) 25% of the total number of ordinary shares subject to the option shares on the first anniversary of the grant date and (2) the remaining 75% of the option shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the first anniversary of the grant date occurs and an additional installment vesting on the last day of each of the 35 months thereafter.

*Scheme III*

Grant date: December 5, 2006

Exercise price per share- original: \$4.172

F-53

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(a) Option granted by the company continued**

*Details of the Share Incentive Plans:* continued

Exercise price per share after modification: \$0.01

Expiration date: December 4, 2016

Number of options granted: 620,212

Among the 620,212 Scheme III options granted, 352,000 options were granted to one officer of the Group and the remaining 268,212 options were granted to other employees and directors.

Vesting schedule of the 268,212 options granted to employees and directors:

The option shall become vested as to (1) 25% of the total number of the option shares on the first anniversary of the grant date and (2) the remaining 75% of the Option Shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the first anniversary of the Grant date occurs and an additional installment vesting on the last day of each of the 35 months thereafter.

*Scheme III* continued

Vesting schedule of the 352,000 options granted to the officer:

320,000 shares subject to the options shall become vested as to (1) 25% of such 320,000 ordinary shares on the closing of an initial public offering in an international stock exchange, provided such initial public offering shall occur within 3 years from the grant date, and (2) the remaining 75% of such 320,000 shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the officer starts its employment and an additional installment vesting on the last day of each of the 35 months thereafter. The vesting of the remaining 32,000 shares is conditional upon whether the performance of non-smart card and CA systems business in the fiscal years from 2007 to 2009 can meet certain financial targets. In July 2010, these 32,000 shares were forfeited as the financial targets were not met.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

*(a) Option granted by the company* continued

*Details of the Share Incentive Plans:* continued

Scheme V

Grant date: October 5, 2008

Exercise price per share original: \$7.89

Exercise price per share after modification: \$3.03

Expiration date: October 4, 2018

Number of options granted: 406,776

Vesting schedule: (1) 25% of the total number of the option shares on the first anniversary of the grant date and (2) the remaining 75% of the Option Shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the first anniversary of the Grant date occurs and an additional installment vesting on the last day of each of the 35 months thereafter.

*Scheme VI*

Grant date: June 2, 2009

Exercise price per share original: \$9.09

Exercise price per share after modification: \$4.23

Expiration date: June 1, 2019

Number of options granted: 357,548

Vesting schedule: (1) 25% of the total number of the option shares on the first anniversary of the grant date and (2) the remaining 75% of the Option Shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the first anniversary of the Grant date occurs and an additional installment vesting on the last day of each of the 35 months thereafter.



**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

*(a) Option granted by the company* continued

*Details of the Share Incentive Plans:* continued

*Scheme VIII*

Grant date: November 15, 2010

Exercise price per share original: \$6.96

Exercise price per share after modification: \$2.10

Expiration date: November 14, 2020

Number of options granted: 50,000

Vesting schedule: The vesting of the options is conditional upon whether the performance of the optionee in the four years after the option grant can meet certain performance targets.

*Scheme IX*

Grant date: November 19, 2010

Exercise price per share original: \$6.90

Exercise price per share after modification: \$2.04

Expiration date: November 19, 2020

Number of options granted: 1,000,000

Vesting schedule: (1) 25% of the total number of option shares on the first anniversary of the grant date; and (2) the remaining 75% of the option shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following the month in which the first anniversary of the grant date occurs and an additional installment vesting on the last day of each of the 35 months thereafter.

*Scheme X*

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Grant date: May 16, 2011

Exercise price per share- original: \$4.90

Exercise price per share after modification: \$2.04

Expiration date: May 15, 2021

Number of options granted: 1,600,000

Type I under Scheme X:

Number of options granted: 1,457,000

Vesting schedule: (1) 25% of the total number of option shares on November 19, 2011; and (2) the remaining 75% of the option shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following November 19, 2011 and an additional installment vesting on the last day of each of the 35 months thereafter.

F-56

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(a) Option granted by the company continued**

**Details of the Share Incentive Plans: continued**

*Scheme X* continued

**Type II under Scheme X:**

Number of options granted: 143,000

Vesting schedule: The vesting of the options is conditional upon whether the performance of the optionee can meet certain performance targets as of April 1, 2012.

*Scheme XI*

Grant date: September 30, 2011

Exercise price per share original: \$4.34

Exercise price per share after modification: \$2.04

Expiration date: September 29, 2021

Number of options granted: 700,000

Vesting schedule: (1) 25% of the total number of option shares on November 19, 2011; and (2) the remaining 75% of the option shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following November 19, 2011 and an additional installment vesting on the last day of each of the 35 months thereafter.

*Scheme XII*

Grant date: November 19, 2011

Exercise price per share original: \$4.34

Exercise price per share after modification: \$2.04

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Expiration date: November 18, 2021

Number of options granted: 300,000

Vesting schedule: (1) 25% of the total number of option shares immediately on November 19, 2011; and (2) the remaining 75% of the option shares shall vest in 36 substantially equal monthly installments, with the first installment vesting on the last day of the month following November 19, 2011 and an additional installment vesting on the last day of each of the 35 months thereafter.

F-57

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(a) Option granted by the company continued**

*Options granted to non-employees*

The Group granted 40,000 options on May 15, 2007 to an independent director who became the Company's independent director upon the IPO of the Company. These options were exercised during the year ended December 31, 2010.

There were no share options granted to non-employees outstanding as of December 31, 2012.

*Termination of options*

If the grantee ceases to be employed by or ceases to provide services to the Group, (a) the grantee will have until the date that is 30 days after his or her severance date to exercise the options (or portion thereof) to the extent that they were vested on the severance date; (b) the options, to the extent not vested on the severance date, shall terminate on the severance date; (c) the options, to the extent exercisable for the 30-day period following the severance date and not exercised during such period, shall terminate at the close of the business on the last day of the 30-day period.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****20. SHARE-BASED COMPENSATION continued****(a) Option granted by the company continued*****Option exercise***

The option shall be exercisable by the delivery to the secretary of corporation of a written notice, in the form approved by the Group, stating the number of ordinary shares to be purchased pursuant to the option and payment in full for the exercise price of the shares to be purchased in cash, by check or by electronic funds transfer to the Group.

Management used the Black-Scholes option pricing model to estimate the fair value of the following options on their respective grant date with the following assumptions:

|            | Expected price<br>volatility range | Risk-free<br>interest rate range | Expected<br>life range | Expected<br>dividends | Fair value of ordinary<br>share at grant date |
|------------|------------------------------------|----------------------------------|------------------------|-----------------------|---|
| Scheme II  | 50.5%-50.6%                        | 5.77%-5.81%                      | 5.50-6.26              | 1.00%                 | \$3.56  |
| Scheme III | 49.8%-52.4%                        | 5.77%-5.83%                      | 5.28-6.54              | 1.00%                 | \$3.56  |
| Scheme V   | 56.20%                             | 2.92%                            | 6.25                   | 0%                    | \$7.66  |
| Scheme VI  | 51.50%                             | 3.28%                            | 6.25                   | 2.50%                 | \$9.09  |

Management used Binomial model to estimate the fair value of the following options on their respective grant date with the following assumptions:

|             | Expected price<br>volatility range | Risk-free<br>interest rate range | Time<br>to vest | Expected<br>dividends | Fair value of ordinary<br>share at grant date |
|-------------|------------------------------------|----------------------------------|-----------------|-----------------------|---|
| Scheme VIII | 38.91%                             | 3.91%                            | 2.13            | 0%                    | \$6.96  |
| Scheme IX   | 38.89%                             | 3.82%                            | 2.16            | 0%                    | \$7.26  |
| Scheme X    | 45.17%                             | 3.99%                            | 0.88-1.69       | 0%                    | \$6.39  |
| Scheme XI   | 73.61%                             | 3.91%                            | 1.32            | 9%                    | \$3.9   |
| Scheme XII  | 72.80%                             | 3.68%                            | 1.18            | 9%                    | \$3.89  |

The fair value of the option at the grant date was \$2.38, \$1.67, \$4.24, \$3.83, \$2.93-\$2.95, \$3.16, \$3.11-\$3.42, \$1.57-\$1.65 and \$1.54-\$1.62 for each option for Scheme II and Scheme III option plans, Scheme V, Scheme VI, Scheme VIII, Scheme IX, Scheme X, Scheme XI and Scheme XII, respectively.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(a) Option granted by the company continued**

*Option exercise* continued

In calculating the fair value of the options using the Black-Scholes or Binomial option pricing model, the following major assumptions were used:

(1) Volatility

For options granted prior to 2011, the volatility of the underlying ordinary shares during the life of the options was estimated based on the historical stock prices volatility of listed comparable companies over a period comparable to the expected term of the options. For options granted since 2011, volatility of the underlying ordinary shares during the life of the options was estimated based on the historical stock price volatility of the Company's own historical stock price volatility over the past years.

(2) Risk free interest rate

Risk free interest rate was estimated based on the yield to maturity of government bonds with a maturity period close to the expected term of the options.

(3) Expected term

The Company estimated the expected term as the average between the vesting term of the options and the original contractual term.

(4) Time to vest

The Company estimated the time to vest as the weighted average remaining vesting period of the options based on the vesting schedule of the options.

(5) Dividend yield

The dividend yield was estimated by the Company based on its expected dividend policy over the expected term of the options and its historical special cash dividend payments.

(6) Exercise price

The exercise price of the options was determined by the Company's board of directors.

(7) Fair value of underlying ordinary shares

The fair value of ADSs representing its ordinary shares on the grant date is determined by the closing trade price of ordinary shares on the grant date.

F-60

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****20. SHARE-BASED COMPENSATION continued****(a) Option granted by the company continued***Option exercise* continued

A summary of stock option activity is as follows:

|   | Number of options | Weighted average exercise price |
|---|-------------------|---------------------------------|
| Options outstanding as at January 1, 2011   | 2,015,381         | \$ 4.43                         |
| Granted                                     | 2,600,000         | 4.34                            |
| Exercised                                   | (163,903)         | 2.12                            |
| Forfeited                                   | (73,915)          | 5.43                            |
| Options outstanding as at December 31, 2011 | 4,377,563         | 2.2*                            |
| Granted                                     |                   |                                 |
| Exercised                                   | (118,864)         | 0.01                            |
| Forfeited                                   | (72,300)          | 2.09                            |
| Options outstanding as at December 31, 2012 | 4,186,399         | 2.26                            |
| Options exercisable as at December 31, 2012 | 1,903,286         | 2.27                            |

\* The weighted average exercise price per option as of December 31, 2011 was retrospectively adjusted to reflect the impact of the exercise price modification in November 2012.

The following table summarizes information with respect to share options outstanding at December 31, 2012:

|             | Weighted-average exercise price | Number outstanding | Number exercisable | Weighted-average remaining contractual life | Intrinsic value |
|-------------|---------------------------------|--------------------|--------------------|---|-----------------|
| Scheme II   | \$ 0.01                         | 6,003              | 6,003              | 3.72 years                                  | \$ 1.67         |
| Scheme III  | 0.01                            | 14,806             | 14,806             | 3.92 years                                  | 1.67            |
| Scheme V    | 3.03                            | 282,876            | 148,434            | 5.76 years                                  |                 |
| Scheme VI   | 4.23                            | 311,914            | 159,912            | 6.42 years                                  |                 |
| Scheme VIII | 2.10                            | 50,000             |                    | 7.88 years                                  |                 |

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|            |      |           |           |            |
|------------|------|-----------|-----------|------------|
| Scheme IX  | 2.04 | 1,000,000 | 520,834   | 7.89 years |
| Scheme X   | 2.04 | 1,567,800 | 711,624   | 8.37 years |
| Scheme XI  | 2.04 | 678,000   | 292,189   | 8.75 years |
| Scheme XII | 2.04 | 275,000   | 49,484    | 8.88 years |
|            |      | 4,186,399 | 1,903,286 |            |

F-61

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****20. SHARE-BASED COMPENSATION continued****(a) Option granted by the company continued***Option exercise* continued

The weighted-average grant-date/ modification date fair value of options granted during the years of 2010 and 2011 was \$3.61 and \$2.66, respectively.

The aggregate intrinsic value of options outstanding, vested and exercisable as of December 31, 2012 was \$35, \$35 and \$35, respectively. The total intrinsic value of options exercised during the years ended December 31, 2010, 2011 and 2012 was \$5,116, \$288 and \$199, respectively.

A summary of unvested stock option activity as of December 31, 2012, and changes during the year ended December 31, 2012 are presented below:

| Unvested Stock Option         | Number of<br>Shares | Weighted average<br>Grant-date Fair Value |
|-------------------------------|---------------------|---|
| Unvested at January 1, 2012   | 2,881,417           | \$ 2.88                                   |
| Granted                       |                     |   |
| Vested                        | (1,140,548)         | 2.99                                      |
| Forfeited                     | (41,933)            | 2.03                                      |
| Unvested at December 31, 2012 | 1,698,936           | \$ 2.83                                   |

The Group recorded the share-based compensation expense of \$1,478, \$5,562 and \$2,503 for the years ended December 31, 2010, 2011 and 2012, respectively.

As of December 31, 2012, total unrecognized compensation expense related to the unvested share options was \$1,457, which is expected to be recognized over a weighted-average period of 1.2 years according to the graded vesting schedule. Total fair value of stock options vested during the year ended December 31, 2010, 2011 and 2012 was \$1,653, \$3,277 and \$3,437, respectively.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****20. SHARE-BASED COMPENSATION continued****(b) Option granted by Cyber Cloud**

On January 18, 2012, Cyber Cloud, a majority-owned subsidiary of the Group, approved the Cyber Cloud 2012 Stock Incentive Plan, under which Cyber Cloud granted 551,000 options to its employees. The share option plan has a term of ten years, which will expire on January 17, 2022 unless terminated earlier by its shareholders and board of directors. The exercise price of the options is \$0.17 per share.

The following table summarizes the Cyber Cloud's share option activities with employees:

|   | Number of options | Weighted average<br>exercise price |
|---|-------------------|------------------------------------|
| Options outstanding as at January 1, 2012   |                   | \$                                 |
| Granted                                     | 551,000           | 0.17                               |
| Exercised                                   |                   |                                    |
| Forfeited                                   | (73,000)          | 0.17                               |
| Options outstanding as at December 31, 2012 | 478,000           | 0.17                               |
| Options exercisable as at December 31, 2012 | 109,542           | 0.17                               |

The fair value of options granted was \$0.23, measured on the grant date based on the Binomial option pricing model with the following assumptions:

|                         |          |
|-------------------------|----------|
| Risk-free interest rate | 3.44%    |
| Expected life (years)   | 10 years |
| Expected dividend yield |          |
| Volatility              | 54.9%    |

In calculating the fair value of the options using the Binomial option pricing model, the following major assumptions were used:

**(1) Volatility**

The volatility of the underlying ordinary shares during the life of the options was estimated based on the historical stock prices volatility of listed comparable companies over a period comparable to the expected term of the options.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(b) Option granted by Cyber Cloud continued**

(2) Risk free interest rate

Risk free interest rate was estimated based on the yield to maturity of government bonds with a maturity period close to the expected term of the options.

(3) Expected term

Cyber Cloud estimated the expected term as the average between the vesting term of the options and the original contractual term.

(4) Time to vest

Cyber Cloud estimated the time to vest as the weighted average remaining vesting period of the options based on the vesting schedule of the options.

(5) Dividend yield

The dividend yield was estimated by Cyber Cloud based on its expected dividend policy over the expected term of the options and its historical special cash dividend payments.

(6) Exercise price

The exercise price of the options was determined by Cyber Cloud's board of directors.

(7) Fair value of underlying ordinary shares

The estimated fair value of the ordinary shares underlying the options as of the grant date was determined based on a retrospective valuation.

Vesting schedule: all options will vest equally in 48 months after the grant date.

Cyber Cloud recorded share-based compensation expense of \$52 for the year ended December 31, 2012.

As of December 31, 2012, total unrecognized compensation expense related to the unvested share options was \$64, which is expected to be recognized over a weighted-average period of 1.58 years according to the graded vesting schedule.



**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****20. SHARE-BASED COMPENSATION continued****(c) Option granted by Joysee**

On February 17, 2012, Joysee, a majority-owned subsidiary of the Group, approved the Joysee 2012 Stock Incentive Plan, under which Joysee granted 520,000 options to its employees. The share option plan has a term of ten years, which will expire on February 16, 2022 unless terminated earlier by its shareholders and board of directors. The exercise price of the options is \$ 0.17 per share.

The following table summarizes the Joysee's share option activities with employees:

|   | Number of<br>options | Weighted average<br>exercise price |
|---|----------------------|------------------------------------|
| Options outstanding as at January 1, 2012   |                      | \$                                 |
| Granted                                     | 520,000              | 0.17                               |
| Exercised                                   |                      |                                    |
| Forfeited                                   | (52,000)             | 0.17                               |
| Options outstanding as at December 31, 2012 | 468,000              | 0.17                               |

Options exercisable as at December 31, 2012

The fair value of options granted was \$0.31, measured on the grant date based on the Binomial option pricing model with the following assumptions:

|                         |          |
|-------------------------|----------|
| Risk-free interest rate | 3.58%    |
| Expected life (years)   | 10 years |
| Expected dividend yield |          |
| Volatility              | 66.29%   |

In calculating the fair value of the options using the Binomial option pricing model, the following major assumptions were used:

**(1) Volatility**

The volatility of the underlying ordinary shares during the life of the options was estimated based on the historical stock prices volatility of listed comparable companies over a period comparable to the expected term of the options.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**20. SHARE-BASED COMPENSATION continued**

**(c) Option granted by Joysee continued**

**(2) Risk free interest rate**

Risk free interest rate was estimated based on the yield to maturity of government bonds with a maturity period close to the expected term of the options.

**(3) Expected term**

Joysee estimated the expected term as the average between the vesting term of the options and the original contractual term.

**(4) Time to vest**

Joysee estimated the time to vest as the weighted average remaining vesting period of the options based on the vesting schedule of the options.

**(5) Dividend yield**

The dividend yield was estimated by Joysee based on its expected dividend policy over the expected term of the options and its historical special cash dividend payments.

**(6) Exercise price**

The exercise price of the options was determined by Joysee's board of directors.

**(7) Fair value of underlying ordinary shares**

The estimated fair value of the ordinary shares underlying the options as of the grant date was determined based on a retrospective valuation.

Vesting schedule: all options will vest equally in 4 years after the grant date.

Joysee recorded share-based compensation expense of \$59 for the year ended December 31, 2012.

As of December 31, 2012, total unrecognized compensation expense related to the unvested share options was \$85, which is expected to be recognized over a weighted-average period of 1.60 years according to the graded vesting schedule.



**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****21. FAIR VALUE MEASUREMENT**Measured at fair value on a recurring basis

The Group's financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2011 included forward contracts, which were classified within Level 2 of the fair value hierarchy because the Company determined the fair value of the forward contracts using discounted cash flow ( DCF ) method with the observable inputs based on the quoted prices for identical assets in markets that are not active, such as the foreign exchange rate as agreed in the forward contracts. There were no such financial assets and liabilities as of December 31, 2012.

The Company did not have Level 1 or Level 3 investments measured at fair value on a recurring basis as of December 31, 2011 and 2012.

The following table summarizes the Group's financial assets and liabilities measured at fair value on recurring basis.

|                   | As of December 31, 2011  |   |  |                  | As of December 31, 2012  |   |  |                  |
|-------------------|--|---|--|------------------|--|---|--|------------------|
|                   | Fair Value Measurements at the Reporting Date  |   |  |                  | Fair Value Measurements at the Reporting Date  |   |  |                  |
|                   | Using  |   |  | Total<br>balance | Using  |   |  | Total<br>balance |
|                   | Quoted prices in<br>active<br>markets<br>for<br>identical<br>instruments<br>(level<br>1) | Significant<br>other<br>observable<br>inputs<br>(level 2) | Significant<br>unobservable<br>inputs<br>(level 3) |                  | Quoted prices in<br>active<br>markets<br>for<br>identical<br>instruments<br>(level<br>1) | Significant<br>other<br>observable<br>inputs<br>(level 2) | Significant<br>unobservable<br>inputs<br>(level 3) |                  |
| Forward contracts | \$   | \$ 404  | \$   | \$ 404           | \$   | \$  | \$   | \$               |

Measured at fair value on a non-recurring basis

The Company measured the fair value of equity method investment in 3Dijoy using income approach-DCF method based on which to recognize the impairment loss in 2012. The equity method investment in 3Dijoy is considered as Level 3 assets because the Company used unobservable inputs, such as weighted average cost of capital ( WACC ) and lack of marketability discount ( LoMD ), to determine the fair value of the equity method investment. The WACC and LoMD used in the fair value measurement were 22% and 40%, respectively. Increase (decrease) in any of WACC and LoMD in isolation can result in lower (higher) fair value measurement.

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 forecast financial performance of the acquired business and discount rates, to determine the fair value of these purchased assets.

Goodwill and intangible assets are measured at fair value on a nonrecurring basis and they are recorded at fair value only when impairment is recognized.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****22. MAINLAND CHINA CONTRIBUTION PLAN**

Full time employees of the Group in the PRC participate in a government-mandated multiemployer defined contribution plan pursuant to which certain pension benefits, medical care, unemployment insurance, employee housing fund and other welfare benefits are provided to employees. PRC labor regulations require the Group to accrue for these benefits based on certain percentages of the employees' salaries. The total contribution for such employee benefits was \$2,805, \$3,365 and \$5,016 for the years ended December 31, 2010, 2011 and 2012, respectively.

**23. COMMITMENTS***Operating lease commitment*

The Group has operating lease agreements principally for its office spaces in the PRC. These leases expire through 2014 and are renewable upon negotiation. Rental expense under operating leases for the years ended December 31, 2010 and 2011 and 2012 was \$1,401, \$1,589 and \$2,443, respectively.

Future minimum lease payments under non-cancelable operating lease agreements are as follows:

|      |          |
|------|----------|
| 2013 | \$ 1,208 |
| 2014 | 315      |
| 2015 |          |
|      | \$1,523  |

*Purchase commitments*

As of December 31, 2012, purchase commitments are \$351, mainly for service.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued****FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012****(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)****24. NONCONTROLLING INTEREST**

|   | Dongguan<br>Super<br>TV<br>(Note 9) | Cyber Cloud<br>(Note 25(c)) | Joysee<br>(Note 24(a)) | Super Movie<br>(Note 24(b)) | Total   |
|---|-------------------------------------|-----------------------------|------------------------|-----------------------------|---------|
| Balance as of January 1, 2010           |                                     |                             |                        |                             |         |
| Acquisition                             | 530                                 |                             |                        |                             | 530     |
| Net loss                                | (10)                                |                             |                        |                             | (10)    |
| Balance as of December 31, 2010         | 520                                 |                             |                        |                             | 520     |
| Capital injection                       |                                     | 759                         | 5,542                  | 236                         | 6,537   |
| Transfer of noncontrolling interest     |                                     |                             | (1,822)                |                             | (1,822) |
| Net income (loss)                       | 105                                 | (221)                       | (491)                  | (123)                       | (730)   |
| Disposal                                | (625)                               |                             |                        |                             | (625)   |
| Balance as of December 31, 2011         |                                     | 538                         | 3,229                  | 113                         | 3,880   |
| Net loss                                |                                     | (402)                       | (870)                  | (117)                       | (1,389) |
| Share-based compensation                |                                     | 5                           | 21                     |                             | 26      |
| Foreign currency translation adjustment |                                     | 30                          | 157                    | 1                           | 188     |
| Balance as of December 31, 2012         |                                     | 171                         | 2,537                  | (3)                         | 2,705   |

- a. Pursuant to an agreement, dated April 29, 2011, between Super TV and Beijing Ying Zhi Cheng Technology Co., Ltd. ( Ying Zhi Cheng Technology ), to establish Joysee in Beijing mainly engaging in the research and development of advanced digital television terminals. Super TV and Ying Zhi Cheng Technology contributed cash of \$4,154 and \$462, representing 90% and 10% of the equity interest in Joysee, respectively.

Pursuant to an agreement, dated May 24, 2011, among Super TV, N-S Digital TV and Ying Zhi Cheng Technology, N-S Digital TV contributed cash of \$923, representing a 16.7% equity interest in Joysee.

Pursuant to an agreement, dated June 13, 2011, among Super TV, N-S Digital TV, Ying Zhi Cheng Technology and Intel Semiconductor (Dalian) Ltd. ( Intel ), Intel contributed \$5,080 in cash, representing a 37.5% equity interest in Joysee. Pursuant to an equity transfer agreement, dated June 13, 2011, between N-S Digital TV and Intel, Intel transferred 7.5% of its equity investment in Joysee to N-S Digital TV for a nominal consideration.

- b. Pursuant to a shareholder investment agreement, dated August 26, 2011, between Super TV and Beijing Chaoying Weichuang Technology Ltd., the parties agreed to establish Super Movie, which mainly engages in video program delivery services. Super TV and Beijing Chaoying Weichuang Technology Ltd. contributed cash in the amount of \$2,111 and \$236, respectively, representing 90% and 10% of the equity interest in Super Movie, respectively.



**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**25. RELATED PARTY BALANCES AND TRANSACTIONS**

- a. On February 26, 2010, the Group entered into an agreement with Beijing Shi Xun, to acquire its 90% equity interest in Guangdong R&D for a cash consideration of \$396. On the same day, the Group entered into an agreement with the holder of the remaining 10% equity interest in Guangdong R&D, an independent third party of the Group, for a cash consideration of \$44. Guangdong R&D became a wholly owned subsidiary of the Group after the transaction. At the time of the transaction, Zengxiang Lu, the Company's director, was the president of Guangdong R&D, and Jianhua Zhu, the Company's chairman, was the executive director of Guangdong R&D. 80% of equity interest of Beijing Shi Xun are held by two family members of the Company's two major shareholders.
- b. In August 2010, the Group entered into an agreement with Rujia, an equity method investee of the Group, to sell 100% equity interest in Guangdong SuperTV Digital Media Co., Ltd. ( Guangdong SuperTV ) at a total consideration of \$4,585. Gain of \$32 generated from the disposal of the investment in Guangdong SuperTV was recorded in income from equity method investments in the consolidated statements of operations in 2010.

As the Group still has significant continuing involvement in the operations of Guangdong SuperTV through Rujia after the above transaction, disposal of Guangdong SuperTV was not considered as discontinued business.

For the year ended December 31, 2012, the Group made purchase of certain media information system amounted to \$290 from Rujia, of which \$233 was not paid as of December 31, 2012.

- c. In December 2010, the Group entered into an agreement with Beijing Yuewu Yuntian Software Technology Ltd. ( Yuewu Yuntian ), which was established by one of the management of the Company, to set up Cyber Cloud that engages in research and development of cloud computing technology and operation. The Group and Yuewu Yuntian contributed cash of \$6,818 and \$759, respectively, in December 2010, representing 90% and 10% of the equity interest in Cyber Cloud. Cyber Cloud was legally established on January 19, 2011.

**Table of Contents**

**CHINA DIGITAL TV HOLDING CO., LTD.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued**

**FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012**

**(U.S. DOLLARS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)**

**26. STATUTORY RESERVES AND RESTRICTED NET ASSETS**

As stipulated by the relevant law and regulations in the PRC, the Company's subsidiary, VIE and VIE's subsidiaries in the PRC are required to maintain non-distributable statutory reserve. Appropriations to the statutory reserve are required to be made at 10% of profit after taxes as reported in these entities' statutory financial statements prepared under PRC GAAP. Once appropriated, these amounts are not available for future distribution to owners or shareholders. Once the statutory reserve is accumulated to 50% of these entities' registered capital, these entities can choose not to provide further statutory reserves. The statutory reserve may be applied against prior year losses, if any, and may be used for general business expansion and production and an increase in registered capital of these entities. Amounts contributed to the statutory reserve were \$4,633, \$370 and \$162 for 2010, 2011 and 2012, respectively.

Relevant PRC laws and regulations restrict the Wholly Foreign Owned Entity ( WFOE ) and VIE from transferring a portion of their net assets, equivalent to the balance of their statutory reserves and their share capital, to the Company in the form of loans, advances or cash dividends. The balance of restricted net assets was \$92,567 and \$92,729, of which \$34,123 and \$34,196 was attributed to the paid in capital and statutory reserves of the VIE and \$58,444 and \$58,533 was attributed to the paid in capital and statutory reserves of the WFOE, as of December 31, 2011 and 2012, respectively. The WFOE's accumulated profits may be distributed as dividends to the Company without the consent of a third party. The VIE's revenues and accumulated profits may be transferred to the Company through contractual arrangements without the consent of a third party. Under applicable PRC law, loans from PRC companies to their offshore affiliated entities require governmental approval, and advances by PRC companies to their offshore affiliated entities must be supported by bona fide business transactions.

**27. SUBSEQUENT EVENT**

In January 2013, the Group granted options to purchase 1,200,000 ordinary shares to employees and directors with the exercise price of \$1.18. The vesting term is: (1) twenty five percent (25%) shall vest on January 8, 2013; (2) the remaining 75% shall vest in 36 substantially equal monthly installments with the first installment vesting on February 28, 2013 and an additional installment vesting on the last day of each of the 35 months thereafter.

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****Additional Information-Financial Statement Schedule I****Condensed Financial Information of Parent Company****BALANCE SHEETS****(U.S. dollars in thousands, except share and per share data)**

|  | As of December 31, |                   |
|--|--------------------|-------------------|
|  | 2011               | 2012              |
| <b>ASSETS</b>  |                    |                   |
| Current assets:  |                    |                   |
| Cash and cash equivalents  | \$ 7,132           | \$ 4,918          |
| Accounts due from subsidiaries, VIE and VIE s subsidiaries-current     | 997                | 1,238             |
| Dividend receivable  |                    | 26,501            |
| Prepaid expenses and other current assets                              | 90                 | 102               |
| <b>Total current assets</b>  | <b>8,219</b>       | <b>32,759</b>     |
| Accounts due from subsidiaries, VIE and VIE s subsidiaries-non-current | 90,480             | 58,090            |
| Long-term investments equity method investments                        | 5,065              |                   |
| Investment in subsidiaries and VIE                                     | 137,113            | 68,235            |
| Deferred tax assets non-current  | 69                 | 138               |
| <b>Total assets</b>  | <b>240,946</b>     | <b>159,222</b>    |
| <b>TOTAL LIABILITIES AND EQUITY</b>                                    |                    |                   |
| Current liabilities:   |                    |                   |
| Accrued expenses and other current liabilities                         | 468                | 670               |
| Deferred revenue-current   | 864                | 1,095             |
| Dividend payable   | 33,172             | 76,999            |
| <b>Total current liabilities</b>                                       | <b>34,504</b>      | <b>78,764</b>     |
| <b>Total Liabilities</b>   | <b>34,504</b>      | <b>78,764</b>     |
| Equity:  |                    |                   |
| Ordinary shares  | 29                 | 30                |
| Additional paid-in capital   | 126,583            | 29,724            |
| Retained earnings  | 54,095             | 24,621            |
| Accumulated other comprehensive income                                 | 25,735             | 26,083            |
| <b>Total shareholders equity</b>                                       | <b>206,442</b>     | <b>80,458</b>     |
| <b>TOTAL LIABILITIES AND EQUITY</b>                                    | <b>\$ 240,946</b>  | <b>\$ 159,222</b> |

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****Additional Information-Financial Statement Schedule I****Condensed Financial Information of Parent Company****STATEMENTS OF COMPREHENSIVE INCOME****(U.S. dollars in thousands, except share and per share data)**

|  | For the years ended December 31, |            |            |
|--|----------------------------------|------------|------------|
|  | 2010                             | 2011       | 2012       |
| Operating expenses   | \$ (2,118)                       | \$ (5,830) | \$ (2,822) |
| Interest income  | 759                              | 37         | 10         |
| Impairment loss on long-term investments                       | (5,000)                          |            | (4,487)    |
| Loss from equity method investment                             | (174)                            | (761)      | (578)      |
| Equity in earnings of subsidiaries, VIE and VIE s subsidiaries | 39,954                           | 47,726     | 14,191     |
| Other income   |                                  |            | 820        |
| Net income before provision for income taxes                   | 33,421                           | 41,172     | 7,134      |
| Provision for income taxes - current                           |                                  | (129)      | (276)      |
| Provision for income taxes - deferred                          |                                  | (43)       | 69         |
| Net income attributable to ordinary shareholders               | \$ 33,421                        | \$ 41,000  | \$ 6,927   |
| Other comprehensive income, net of tax                         |                                  |            |            |
| Foreign currency translation adjustment                        | 6,943                            | 12,175     | 348        |
| Comprehensive income attributable to ordinary shareholders     | \$ 40,364                        | \$ 53,175  | \$ 7,275   |

F-73

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****Additional Information-Financial Statement Schedule I****Condensed Financial Information of Parent Company****STATEMENTS OF CHANGES IN EQUITY****(U.S. dollars in thousands, except share and per share data)**

|   | Ordinary   |        | Additional<br>paid-in<br>capital | Accumulated<br>other<br>comprehensive<br>income | Retained<br>earning | Total<br>equity |
|---|------------|--------|----------------------------------|---|---------------------|-----------------|
|   | Shares     | Amount |                                  |   |                     |                 |
| Balance at January 1, 2010              | 58,044,640 | \$ 29  | \$ 157,980                       | \$ 6,617  | \$ 88,398           | \$ 253,024      |
| Share-based compensation                |            |        | 1,478                            |   |                     | 1,478           |
| Exercise of stock option                | 773,347    |        | 1,270                            |   |                     | 1,270           |
| Special cash dividend to shareholders   |            |        | (41,929)                         |   | (75,707)            | (117,636)       |
| Net income                              |            |        |                                  |   | 33,421              | 33,421          |
| Foreign currency translation adjustment |            |        |                                  | 6,943   |                     | 6,943           |
| Balance at December 31, 2010            | 58,817,987 | 29     | 118,799                          | 13,560  | 46,112              | 178,500         |
| Share-based compensation                |            |        | 5,562                            |   |                     | 5,562           |
| Exercise of stock option                | 163,903    |        | 400                              |   |                     | 400             |
| Special cash dividend to shareholders   |            |        |                                  |   | (33,017)            | (33,017)        |
| Transfer of noncontrolling interest     |            |        | 1,822                            |   |                     | 1,822           |
| Net income                              |            |        |                                  |   | 41,000              | 41,000          |
| Foreign currency translation adjustment |            |        |                                  | 12,175  |                     | 12,175          |
| Balance at December 31, 2011            | 58,981,890 | 29     | 126,583                          | 25,735  | 54,095              | 206,442         |
| Share-based compensation                |            |        | 2,588                            |   |                     | 2,588           |
| Exercise of stock option                | 118,864    | 1      | 85                               |   |                     | 86              |
| Special cash dividend to shareholders   |            |        | (99,532)                         |   | (36,401)            | (135,933)       |
| Net income                              |            |        |                                  |   | 6,927               | 6,927           |
| Foreign currency translation adjustment |            |        |                                  | 348   |                     | 348             |
| Balance at December 31, 2012            | 59,100,754 | \$ 30  | \$ 29,724                        | \$ 26,083                                       | \$ 24,621           | \$ 80,458       |

**Table of Contents****CHINA DIGITAL TV HOLDING CO., LTD.****Additional Information-Financial Statement Schedule I****Condensed Financial Information of Parent Company****STATEMENTS OF CASH FLOWS****(U.S. dollars in thousands, except share and per share data)**

|  | For the years ended December 31, |                 |                 |
|--|----------------------------------|-----------------|-----------------|
|  | 2010                             | 2011            | 2012            |
| Net cash provided by operating activities                    | \$ 17,554                        | \$ 59,956       | \$ 88,986       |
| Net cash provided by investing activities                    | 3,652                            | 1,152           | 820             |
| Net cash used in financing activities                        | (39,033)                         | (76,779)        | (92,020)        |
| Effect of exchange rate changes on cash and cash equivalents | 6,943                            |                 |                 |
| <b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>             | <b>(10,884)</b>                  | <b>(15,671)</b> | <b>(2,214)</b>  |
| CASH AND CASH EQUIVALENTS, BEGINNING OF THE YEAR             | 33,687                           | 22,803          | 7,132           |
| <b>CASH AND CASH EQUIVALENTS, END OF THE YEAR</b>            | <b>\$ 22,803</b>                 | <b>\$ 7,132</b> | <b>\$ 4,918</b> |

Note:

**Basis for preparation**

The parent-company financial information of China Digital TV Holding Co., Ltd. has been prepared using the same accounting policies as set out in the Group's consolidated financial statements except that China Digital TV Holding Co., Ltd. has used equity method to account for its investments in its subsidiaries and variable interest entity.

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

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 1.1 <sup>(1)</sup>  | Second Amended and Restated Memorandum and Articles of Association of China Digital TV Holding Co., Ltd.   |
| 2.1 <sup>(1)</sup>  | Specimen of Share Certificate.   |
| 2.2 <sup>(1)</sup>  | Form of Deposit Agreement, including form of American Depositary Receipts.   |
| 2.3 <sup>(1)</sup>  | First Amended and Restated Shareholders Agreement of China Digital TV Holding Co., Ltd., dated September 13, 2007, among Novel-Tongfang Information Engineering Co., Ltd., Beijing Novel-Tongfang Digital TV Technology Co., Ltd., China Digital TV Technology Co., Ltd., China Capital Investment Holdings Limited, China Cast Investment Holdings Limited, SB Asia Infrastructure Fund L.P., Capital International Private Equity Fund IV, L.P., CGPE IV, L.P. and certain other shareholders. |
| 4.1 <sup>(1)</sup>  | Asset Transfer Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd.  |
| 4.2 <sup>(1)</sup>  | Equity Transfer Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd. and related (i) Equity Entrustment Agreement, dated September 10, 2004, and (ii) Equity Purchase Entrustment Agreement, dated April 1, 2004, both between the same parties.   |
| 4.3 <sup>(1)</sup>  | Asset Purchase Agreement, dated June 8, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.4 <sup>(1)</sup>  | Equity Transfer Agreement, dated August 4, 2006, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and related Equity Transfer Agreement, dated March 15, 2007, among Novel-Tongfang Information Engineering Co., Ltd., Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Panasonic Corporation of China.   |
| 4.5 <sup>(1)</sup>  | Asset Transfer Agreement, dated August 5, 2006, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and the Supplemental Agreement thereto, dated April 6, 2007.   |
| 4.6 <sup>(1)</sup>  | Trademark Licensing Agreement entered into in March 2007 between Beijing Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd.   |
| 4.7 <sup>(1)</sup>  | Equipment Leasing Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.8 <sup>(1)</sup>  | Technical Support and Related Service Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.9 <sup>(1)</sup>  | Technology License Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.10 <sup>(1)</sup> | Technology Development Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.11 <sup>(1)</sup> | Products and Software Purchase Agreement, dated June 7, 2004, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.  |
| 4.12 <sup>(3)</sup> | Letter of Consent, dated April 30, 2009, issued by Beijing Super TV Co., Ltd. to Beijing Novel-Super Digital TV Technology Co., Ltd.   |
| 4.13 <sup>(3)</sup> | Equity Transfer Agreement, dated June 20, 2008 between Wei Gao and Junming Wu for Beijing Novel-Super Digital TV Technology Co., Ltd.  |
| 4.14 <sup>(3)</sup> | Equity Transfer Agreement, dated November 24, 2008, between Novel-Tongfang Information Engineering Co., Ltd. and Shizhou Shen for Beijing Novel-Super Digital TV Technology Co., Ltd.  |
| 4.15 <sup>(3)</sup> | Equity Transfer Agreement, dated November 24, 2008, between Novel-Tongfang Information Engineering Co., Ltd. and Lei Zhang for Beijing Novel-Super Digital TV Technology Co., Ltd.   |
| 4.16                | Equity Transfer Option Agreement, dated June 7, 2004, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Li Yang <sup>(1)</sup> ; the Supplemental Agreement thereto, dated September 1, 2005, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. <sup>(1)</sup> ; the No. 2 Supplemental Agreement thereto, dated August 18, 2007, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang, Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Wei Gao <sup>(1)</sup> ; the No. 3 Supplemental Agreement thereto, dated June 20, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Wei Gao and Junming Wu <sup>(3)</sup> ; the No. 4 Supplemental Agreement thereto, dated November 24, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Junming Wu, Lei Zhang and Shizhou Shen <sup>(3)</sup> ; and the No. 5 Supplemental Agreement thereto, dated July 11, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang <sup>(6)</sup> . |
| 4.17 <sup>(1)</sup> | Share Pledge Agreement, dated September 1, 2005, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.18 <sup>(3)</sup> | Termination Agreement of Share Pledge, dated November 24, 2008, between Beijing Super TV Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd.  |
| 4.19                | Share Pledge Agreement, dated September 1, 2005, between Li Yang and Beijing Super TV Co., Ltd. <sup>(1)</sup> ; the Supplemental Agreement thereto, dated August 18, 2007, among Li Yang, Beijing Super TV Co., Ltd. and Wei Gao <sup>(1)</sup> ; the No. 2 Supplemental Agreement thereto, dated June 20, 2008, among Beijing Super TV Co., Ltd., Wei Gao and Junming Wu <sup>(3)</sup> ; and the Share Pledge Termination Agreement, dated July 11, 2011 between Beijing Super TV Co., Ltd. and Junming Wu <sup>(6)</sup> .   |
| 4.20 <sup>(3)</sup> | Share Pledge Agreement, dated November 24, 2008, between Shizhou Shen and Beijing Super TV Co., Ltd.   |
| 4.21 <sup>(3)</sup> | Share Pledge Agreement, dated November 24, 2008, between Lei Zhang and Beijing Super TV Co., Ltd.  |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.22                | Business Operating Agreement, dated September 1, 2005, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang and Beijing Novel-Tongfang Digital TV Technology Co., Ltd. <sup>(1)</sup> ; the Supplemental Agreement thereto, dated August 18, 2007, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Li Yang, Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Wei Gao <sup>(1)</sup> ; the No. 2 Supplemental Agreement thereto, dated June 20, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Wei Gao and Junming Wu <sup>(3)</sup> ; the No. 3 Supplemental Agreement thereto, dated November 24, 2008, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd., Junming Wu, Lei Zhang and Shizhou Shen <sup>(3)</sup> ; and the No. 4 Supplemental Agreement thereto, dated July 11, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang <sup>(6)</sup> . |
| 4.23 <sup>(1)</sup> | Power of Attorney, dated September 1, 2005, of Novel-Tongfang Information Engineering Co., Ltd.  |
| 4.24 <sup>(1)</sup> | Power of Attorney, dated August 18, 2007, of Wei Gao.  |
| 4.25 <sup>(3)</sup> | Power of Attorney, dated June 20, 2008, of Junming Wu.   |
| 4.26 <sup>(3)</sup> | Power of Attorney, dated November 24, 2008, of Shizhou Shen.   |
| 4.27 <sup>(3)</sup> | Power of Attorney, dated November 24, 2008, of Lei Zhang.  |
| 4.28 <sup>(1)</sup> | Entrusted Loan Agreement, dated August 23, 2004, among Beijing Super TV Co., Ltd., Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.29 <sup>(1)</sup> | Entrusted Loan Agreement, dated July 13, 2004, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.30 <sup>(1)</sup> | Entrusted Loan Agreement, dated August 25, 2005, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.31 <sup>(1)</sup> | Loan Agreement, dated April 4, 2007, between Beijing Super TV Co., Ltd. and Novel-Tongfang Information Engineering Co., Ltd. and the related Entrusted Loan Agreement, dated April 12, 2007, among Beijing Super TV Co., Ltd., Novel-Tongfang Information Engineering Co., Ltd. and Bank of Beijing, Shangdi Branch.   |
| 4.32 <sup>(3)</sup> | Loan Agreement, dated November 24, 2008, between Shizhou Shen and Beijing Super TV Co., Ltd.   |
| 4.33 <sup>(3)</sup> | Loan Agreement, dated November 24, 2008, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.34 <sup>(1)</sup> | Service Agreement, dated April 2, 2007, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Novel-Tongfang Digital TV Technology Co., Ltd.  |
| 4.35 <sup>(1)</sup> | Interest Payment Agreement, dated November 30, 2006, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.36 <sup>(1)</sup> | Form of Property Lease Agreement.  |
| 4.37 <sup>(1)</sup> | Fixed Assets Transfer Agreement, dated March 28, 2007, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Beijing Super TV Co., Ltd.   |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.38 <sup>(1)</sup> | Form of Employment Agreement and related Form of Agreement on Confidentiality and Intellectual Property.   |
| 4.39 <sup>(1)</sup> | Form of Non-Disclosure, Non-Competition, Commitment and Proprietary Information Agreement.   |
| 4.40 <sup>(1)</sup> | Form of Indemnification Agreement for Directors.   |
| 4.41 <sup>(1)</sup> | Amended and Restated 2005 Stock Incentive Plan of China Digital TV Holding Co., Ltd. and form of share option agreement.   |
| 4.42 <sup>(1)</sup> | Cooperation Agreement, dated January 5, 2007, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and Jiangsu Qingda Science and Technology Industries Co., Ltd.                          |
| 4.43 <sup>(1)</sup> | Cooperation Agreement, dated July 18, 2007, between Beijing Novel-Tongfang Digital TV Technology Co., Ltd. and China Electronics Smart Card Co., Ltd.  |
| 4.44 <sup>(1)</sup> | 2008 Stock Incentive Plan of China Digital TV Holding Co., Ltd.  |
| 4.45 <sup>(2)</sup> | Agreement for Equity Transfer of Beijing Novel-Super Digital TV Technology Co., Ltd., dated December 2007, between China Digital TV Technology Co., Ltd. and Golden Benefit Technology Co., Ltd.     |
| 4.46 <sup>(3)</sup> | Intellectual Property Transfer Agreement, dated August 13, 2008, between Novel-Tongfang Information Engineering Co., Ltd. and Beijing Super TV Co., Ltd.   |
| 4.47 <sup>(3)</sup> | Equity Transfer Agreement, dated October 5, 2008, between Beijing Super TV Co., Ltd. and Beijing Novel-Super Digital TV Technology Co., Ltd.   |
| 4.48 <sup>(3)</sup> | Framework Agreement for Purchase of Computer Chips, dated December 12, 2008, between Beijing Super TV Co., Ltd. and Beijing Novel-Super Digital TV Technology Co., Ltd.                              |
| 4.49 <sup>(4)</sup> | Framework Agreement for Sale of Software Products, dated July 14, 2009, between Beijing Super TV Co., Ltd. and Beijing Novel-Super Digital TV Technology Co., Ltd.                                   |
| 4.50 <sup>(4)</sup> | Equity Transfer Agreement, dated February 26, 2010, between Beijing Novel-Super Digital TV Technology Co., Ltd. and Beijing Shi Xun Hu Lian Technology Co., Ltd.                                     |
| 4.51 <sup>(5)</sup> | Shareholders Agreement, dated December 1, 2010, between Beijing Super TV Co., Ltd. and Beijing Yuewu Yuntian Software Technology Co., Ltd.   |
| 4.52 <sup>(5)</sup> | Shareholders Agreement, dated April 29, 2011, between Beijing Super TV Co., Ltd. and Beijing Ying Zhi Cheng Technology Co., Ltd.   |
| 4.53 <sup>(5)</sup> | 2010 Stock Incentive Plan of China Digital TV Holding Co., Ltd.  |
| 4.54 <sup>(6)</sup> | Loan Agreement, dated July 11, 2011, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.55 <sup>(6)</sup> | Loan Agreement, dated July 11, 2011, between Tianxing Wang and Beijing Super TV Co., Ltd.  |
| 4.56 <sup>(6)</sup> | Loan Agreement, dated July 11, 2011, between Wenjun Wang and Beijing Super TV Co., Ltd.  |
| 4.57 <sup>(6)</sup> | Capital Increase and Equity Transfer Agreement, dated July 11, 2011, between Junming Wu, Lei Zhang, Shizhou Shen, Wenjun Wang, Tianxing Wang and Beijing Novel-Super Digital TV Technology Co., Ltd. |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.58 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Lei Zhang.  |
| 4.59 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Shizhou Shen.   |
| 4.60 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Tianxing Wang.  |
| 4.61 <sup>(6)</sup> | Power of Attorney, dated July 11, 2011, of Wenjun Wang.  |
| 4.62 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Lei Zhang and Beijing Super TV Co., Ltd.  |
| 4.63 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Shizhou Shen and Beijing Super TV Co., Ltd.   |
| 4.64 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Tianxing Wang and Beijing Super TV Co., Ltd.  |
| 4.65 <sup>(6)</sup> | Share Pledge Agreement, dated July 11, 2011, between Wenjun Wang and Beijing Super TV Co., Ltd.  |
| 4.66 <sup>(6)</sup> | Written Undertaking, dated November 22, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang.   |
| 4.67 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Lei Zhang.   |
| 4.68 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Shizhou Shen.  |
| 4.69 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Tianxing Wang.   |
| 4.70 <sup>(6)</sup> | Power of Attorney, dated January 16, 2012, of Wenjun Wang.   |
| 4.71 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Lei Zhang and Beijing Super TV Co., Ltd.   |
| 4.72 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Shizhou Shen and Beijing Super TV Co., Ltd.  |
| 4.73 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Tianxing Wang and Beijing Super TV Co., Ltd.   |
| 4.74 <sup>(6)</sup> | Share Pledge Agreement, dated January 16, 2012, between Wenjun Wang and Beijing Super TV Co., Ltd.   |
| 4.75 <sup>(6)</sup> | Supplemental Agreement to Loan Agreements, dated January 16, 2012, among Beijing Super TV Co., Ltd., Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang.                                   |
| 4.76 <sup>(6)</sup> | Supplemental Agreement, dated February 9, 2012, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Lei Zhang, Shizhou Shen, Wenjun Wang and Tianxing Wang. |
| 4.77 <sup>(6)</sup> | Cooperation Termination Agreement, dated November 9, 2011, between Dongguan SuperTV Video Info Co., Ltd. and the Dongguan branch of the Guangdong Broadcasting TV Network Co., Ltd.            |

**Table of Contents**

| <b>Number</b>       | <b>Description of Exhibit</b>  |
|---------------------|--|
| 4.78 <sup>(6)</sup> | Capital Increase Agreement, dated May 24, 2011, among Beijing Super TV Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., Ying Zhi Cheng Technology Co., Ltd. and Beijing Joysee Technology Co., Ltd.   |
| 4.79 <sup>(6)</sup> | First Amendment to First Amended and Restated Shareholders Agreement of China Digital TV Holding Co., Ltd., dated June 14, 2011, among China Digital TV Technology Co., Ltd., Beijing Novel-Super Digital TV Technology Co., Ltd., China Cast Investment Holdings Limited, SB Asia Infrastructure Fund L.P., Capital International Private Equity Fund IV, L.P., CGPE IV, L.P. and certain other shareholders. |
| 4.80                | China Digital TV Holding Co., Ltd. 2012 Stock Incentive Plan   |
| 4.81                | Second Supplemental Agreement to Loan Agreement, dated April 12, 2013, between Beijing Super TV Co., Ltd. and Tianxing Wang.   |
| 8.1                 | List of Subsidiaries of China Digital TV Holding Co., Ltd.   |
| 11.1 <sup>(1)</sup> | Code of Business Conduct and Ethics of China Digital TV Holding Co., Ltd.  |
| 12.1                | CEO Certification pursuant to Rule 13a-14(a).  |
| 12.2                | CFO Certification pursuant to Rule 13a-14(a).  |
| 13.1                | CEO Certification pursuant to Rule 13a-14(b).  |
| 13.2                | CFO Certification pursuant to Rule 13a-14(b).  |
| 23.1                | Consent of Deloitte Touche Tohmatsu Certified Public Accountants LLP.  |
| 23.2                | Consent of Han Kun, PRC Lawyers.   |

Portions of the agreement have been omitted pursuant to a confidential treatment request and have been filed with the SEC separately with a confidential treatment request.

- (1) Previously filed as an exhibit to the Registration Statement on Form F-1 (File No. 333-146072) of China Digital TV Holding Co., Ltd. and incorporated herein by reference thereto.
- (2) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on June 18, 2008 and incorporated herein by reference thereto.
- (3) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on May 20, 2009 and incorporated herein by reference thereto.
- (4) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on April 30, 2010 and incorporated herein by reference thereto.
- (5) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on May 12, 2011 and incorporated herein by reference thereto.
- (6) Previously filed as an exhibit to the annual report on Form 20-F (File No. 001-33692) of China Digital TV Holding Co., Ltd. filed with the SEC on April 17, 2012 and incorporated herein by reference thereto.