

The9 LTD
Form 20-F
April 16, 2010

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

FORM 20-F

(Mark One)

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

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2009
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: 001-34238

THE9 LIMITED
(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)
Building No. 3, 690 Bibo Road
Zhang Jiang Hi-Tech Park
Pudong New Area, Pudong
Shanghai 201203
People's Republic of China
(Address of principal executive offices)

George Lai
Tel: +86-21-5172-9990
Facsimile number: +86-21-5172-9903
Building No. 3, 690 Bibo Road
Zhang Jiang Hi-Tech Park
Pudong New Area, Pudong

Shanghai 201203

People's Republic of China

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

Name of each exchange and title of each class on which registered:

**American Depository Shares, each representing one ordinary share, par value
US\$0.01 per share, Nasdaq Global Market**

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: 25,512,745 ordinary shares, par value US\$0.01 per share as of December 31, 2009.

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

(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

U.S. GAAP

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

Other

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

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

(APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS)

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

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INTRODUCTION

In this annual report, unless otherwise indicated, (1) the terms we, us, our company, our and The9 refer to The9 Limited and its subsidiaries, and, in the context of describing our operations and risk factors, also includes our affiliated PRC entities, (2) the terms shares and ordinary shares refer to our ordinary shares, and ADSs refers to our American Depositary Shares, each of which represents one ordinary share, and ADRs refers to the American Depositary Receipts, which evidence our ADSs, (3) China and PRC refer to the People's Republic of China, and solely for the purpose of this annual report, excluding Taiwan, Hong Kong and Macau, (4) all references to RMB and Renminbi are to the legal currency of China and all references to U.S. dollars, dollars, US\$ and \$ are to the legal currency of the United States, (5) all discrepancies in any table between the amounts identified as total amounts and the sum of the amounts listed therein are due to rounding, and (6) all translations from RMB to U.S. dollars and from U.S. dollars to RMB in this annual report were made at a rate of RMB6.8259 to US\$1.00, the noon buying rate in effect as of December 31, 2009.

This annual report on Form 20-F includes our audited consolidated statements of operations for the years ended December 31, 2007, 2008 and 2009, and consolidated balance sheet data as of December 31, 2008 and 2009. We and certain selling shareholders of our company completed the initial public offering of 6,075,000 ADSs, each representing one ordinary share, par value US\$0.01 per share, on December 20, 2004. On December 15, 2004, we listed our ADSs on the Nasdaq Global Market, or Nasdaq, under the ticker symbol NCTY.

Table of Contents**PART I****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not Applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not Applicable.

ITEM 3. KEY INFORMATION**A. Selected Financial Data**

The following table presents selected consolidated financial information for our company. You should read the following information in conjunction with Item 5. Operating and Financial Review and Prospects below. The selected consolidated statement of operations data for the years ended December 31, 2007, 2008 and 2009 and the selected consolidated balance sheet data as of December 31, 2008 and 2009 have been derived from our audited consolidated financial statements and should be read in conjunction with those statements, which are included in this annual report beginning on page F-1. The selected consolidated statement of operations data for the year ended December 31, 2005 and December 31, 2006 and the selected consolidated balance sheet data as of December 31, 2005, 2006 and 2007 have been derived from our audited consolidated financial statements, which are not included in this annual report.

	For the Year Ended December 31,					
	2005	2006	2007	2008	2009	2009
	RMB	RMB	RMB	RMB	RMB	US\$⁽¹⁾
	<i>(in thousands, except for per share and per ADS data)</i>					
Consolidated Statement of Operation Data:						
Revenues	489,191	1,038,328	1,350,129	1,806,130	802,629	117,586
Sales taxes	(24,164)	(52,502)	(70,522)	(94,639)	(42,113)	(6,170)
Net revenues	465,027	985,826	1,279,607	1,711,491	760,516	111,416
Cost of services	(240,416)	(524,032)	(700,047)	(997,949)	(712,473)	(104,378)
Gross profit	224,611	461,794	579,560	713,542	48,043	7,038
Operating expenses	(164,898)	(191,639)	(343,695)	(578,993)	(530,884)	(77,775)
Profit (loss) from operations	59,713	270,155	235,865	134,549	(482,841)	(70,737)
Interest income, net	10,022	9,136	50,656	56,691	30,501	4,468
Other income (expense), net	14,467	28,417	(30,054)	(18,967)	61,840	9,060
Income (loss) before income taxes, gain on investment disposal, impairment loss on investments and share of loss in equity investments	84,202	307,708	256,467	172,273	(390,500)	(57,209)
Income tax (expense) benefit	(168)	2,670	(9,269)	(47,929)	5,536	811
Income (loss) before gain on investment disposal, impairment loss on investments and share of loss in equity investments	84,034	310,378	247,198	124,344	(384,964)	(56,398)
Gain on investment disposal	6,716	23,409				
Impairment loss on investments		(20,402)	(627)	(25,922)	(22,412)	(3,283)
Share of loss in equity investments, net of taxes	(13,737)	(908)	(5,679)	(2,241)	(2,556)	(374)
Net income (loss)	77,013	312,477	240,892	96,181	(409,932)	(60,055)

Net income (loss) attributable to noncontrolling interest ⁽²⁾	4,541			(655)	(4,780)	(700)
Net income (loss) attributable to holders of ordinary shares	72,472	312,477	240,892	96,836	(405,152)	(59,355)
Net income (loss) attributable to holders of ordinary shares per share						
Basic	3.00	12.78	8.79	3.50	(15.94)	(2.34)
Diluted	2.92	12.72	8.72	3.50	(15.94)	(2.34)
Net income (loss) attributable to holders of ordinary shares per ADS ⁽³⁾						
Basic	3.00	12.78	8.79	3.50	(15.94)	(2.34)
Diluted	2.92	12.72	8.72	3.50	(15.94)	(2.34)

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	2005	2006	As of December 31,		2009	2009
	RMB	RMB	2007	2008	RMB	US\$(¹)
			RMB	RMB		
			<i>(in thousands, except for per share and per ADS data)</i>			
Consolidated Balance Sheet Data:						
Cash and cash equivalents	488,245	937,846	2,215,282	2,152,586	1,675,081	245,401
Non-current assets	602,744	537,492	831,342	769,023	522,161	76,497
Total assets	1,213,735	1,624,585	3,246,101	3,263,009	2,324,958	340,608
Total current liabilities	271,750	288,427	440,011	543,767	311,508	45,636
Total equity	941,985	1,336,158	2,806,090	2,719,242	2,013,450	294,972
Total liabilities and equity	1,213,735	1,624,585	3,246,101	3,263,009	2,324,958	340,608

(1) Translation from RMB amounts into U.S. dollars was made at a rate of RMB6.8259 to US\$1.00. See Exchange Rate Information.

(2) We adopted authoritative guidance regarding accounting for noncontrolling interests on January 1, 2009, retrospectively.

(3) Each ADS represents one ordinary share.

Our license to operate World of Warcraft, or WoW, in China through cooperation with Shanghai The9 Information Technology Co., Ltd. (Shanghai IT, formerly known as Shanghai Jiucheng Information Technology Co. Ltd.), our affiliated entity, was not renewed upon its expiration on June 7, 2009. See Item 5. Operating and Financial Review and Prospects A. Overview Recent Impairment Provisions Related to the Non-renewal of the WoW License below.

Exchange Rate Information

Our business is primarily conducted in China and almost all of our revenues are denominated in RMB. This annual report contains translations of RMB amounts into U.S. dollars based on the noon buying rate in the city of New York for cable transfers of RMB, as certified for customs purposes by the Federal Reserve Bank of New York. For your convenience, this annual report contains translations of some RMB or U.S. dollar amounts for 2009 at US\$1.00: RMB6.8259, which was the noon buying rate in effect as of December 31, 2009. The prevailing rate on April 9, 2010

was US\$1.00: RMB6.8229. We make no representation that any RMB or U.S. dollar amounts could have been, or could be, converted into U.S. dollars or RMB, as the case may be, at any particular rate, the rates stated below, or at all. The PRC government imposes control over its foreign currency reserves in part through direct regulation of the conversion of RMB into foreign currency and through restrictions on foreign exchange activities.

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The following table sets forth information concerning exchange rates between the RMB and the U.S. dollar for the periods indicated. These rates are provided solely for your convenience and are not necessarily the exchange rates that we used in this annual report or will use in the preparation of our other periodic reports or any other information to be provided to you. The source of these rates is the Federal Reserve Bank of New York.

Period	Noon Buying Rate			
	Period End	Average⁽¹⁾	Low	High
2005	8.0702	8.1826	8.2765	8.0702
2006	7.8041	7.9579	8.0702	7.8041
2007	7.2946	7.5806	7.8127	7.2946
2008	6.8225	6.9193	7.2946	6.7800
2009	6.8259	6.8295	6.8470	6.8176
October	6.8264	6.8267	6.8292	6.8248
November	6.8265	6.8271	6.8300	6.8255
December	6.8259	6.8275	6.8299	6.8244
2010				
January	6.8268	6.8269	6.8295	6.8258
February	6.8258	6.8285	6.8330	6.8258
March	6.8258	6.8262	6.8270	6.8254
April (through April 9, 2010)	6.8229	6.8250	6.8263	6.8229

(1) Annual averages are calculated from month-end rates. Monthly averages are calculated using the average of the daily rates during the relevant period.

B. Capitalization and Indebtedness

Not Applicable.

C. Reasons for the Offer and Use of Proceeds

Not Applicable.

D. Risk Factors**Risks Related to Our Company**

If we are unable to successfully establish new relationships with online game developers, and maintain a satisfactory relationship with the online game developers that have licensed games to us, our future results of operations and profitability will be materially impacted.

We rely heavily on our relationships with online game developers that have licensed games to us, such as our relationship with Blizzard Entertainment, Inc. which permitted our subsidiary, China The9 Interactive Limited (C9I), to operate World of Warcraft, or WoW, in China through cooperation with Shanghai IT, our affiliated entity before June 2009. Our agreement with Blizzard Entertainment, Inc., which expired on June 7, 2009, accounted for approximately 91% of our total revenue in 2008 and approximately 88% of our total revenues in 2009. We also rely on our relationships with, among others, game licensors such as EA Swiss Sàrl, Webzen, Inc., G10 Entertainment Corp., Hanbitsoft Inc., Ndoors Corporation and USERJOY Technology Co., Ltd. Our license agreement with Webzen,

Inc. to operate Soul of the Ultimate Nation, or SUN, will expire on May 24, 2010. Our license agreement with Hanbitsoft Inc. and IMC Games Co., Ltd. to operate Granado Espada, or GE, will expire on November 22, 2010. In order for our business strategy to be successful in the near term, we will need to license new online games, as well as develop proprietary games, that are attractive to users. Our results of operations and profitability will be materially impacted if we are unable to license new online games in the future. In addition, if we are unable to maintain a satisfactory relationship with the online game developers that have licensed games to us, or should any of these game licensors either establish similar or more favorable relationships with our competitors in violation of their contractual arrangements with us or otherwise, our operating results and our business would be harmed because our business depends significantly upon our exclusive licenses to operate online games in China. We cannot assure you that any of our online game licensors will renew their license agreements with us, or grant us an exclusive license for any new online games that they may develop or make expansion packs for existing games available to us in the future. Any deterioration in our relationships with our online game licensors could harm our future results of operations or the growth of our business.

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Our business is intensely competitive and hit driven. If we do not deliver new hit products to the market, or if consumers prefer our competitors products or services over those we provide, our operating results will suffer.

We operate in a highly competitive and dynamic market, and our future success depends not only on the popularity of our existing online games but also, in large part, on our ability to develop and introduce new games that are attractive to our customers. To achieve this, we will need to anticipate and effectively adapt to rapidly changing consumer tastes and preferences and technological advances. The development of new games can be very difficult and requires high levels of innovation. We do not have a proven track record with developing proprietary massively multiplayer online role playing games, or MMORPGs, from which we derive a significant portion of our profits. While new products are regularly introduced, only a small number of hit titles account for a significant portion of total revenue in our industry. Hit products offered by our competitors may take a larger share of the market than we anticipate, which could cause revenues generated by our products to fall below expectations. If our competitors develop more successful products, or offer similar products at lower price points or pursuant to payment models viewed as offering a better value than we do, our revenues, margins and profitability will decline.

Also, in order to maintain the life span of our new online games, which we believe is typically four to five years for successful online games or two to three years for most other online games, we need to continue to develop and release upgrades to our new online games. We cannot assure you that we will be able to identify appropriate games or enter into arrangements with those game developers to offer these games in China, on terms acceptable to us or at all, or that we can maintain the expected life span of our new online games. If we are not able to license, develop or acquire additional attractive online games with lasting appeal to users, our future revenues and profitability will decline.

We may not be able to maintain our market share and profitability as we operate in a highly competitive industry and compete against many companies.

There are currently over 100 online game operators in China. We expect that, given the relatively low barriers to entry, more companies will enter the online game industry in China and a wider range of online games will be introduced to the Chinese market. Our competitors vary in size and include large companies, many of which have significantly greater financial, marketing and game development resources and name recognition than we have, such as Shanda Games Limited, Netease.com, Inc., Perfect World Co., Ltd., Tencent Inc., Changyou.com Limited and Giant Interactive Group. As a result, we may not be able to devote adequate resources to designing, developing or acquiring new games, undertaking extensive marketing campaigns, adopting aggressive pricing policies, paying high compensation to game developers or compensating independent game developers to the same degree as certain of our competitors. Our competitors may introduce new business methods. If these new business methods are more attractive to customers than the business methods we currently use, our customers may switch to our competitors games, and we may lose market share. We cannot assure you that we will be able to compete successfully against new or existing competitors, or against new business methods implemented by them. In addition, the increased competition we anticipate in the online game industry may also reduce the number of our users or the growth rate of our user base, reduce the average number of hours played by our users, or cause us to reduce usage fees. All of these competitive factors could adversely affect our operational success, cash flows, operating margins and profitability.

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We are subject to securities class action lawsuits alleging that we and certain of our directors and officers disseminated or approved materially false and misleading statements and failed to disclose that we might not be able to renew the license of WoW. If the class action lawsuits are successful, they may have an adverse effect on our financial condition and operating results.

On October 21, 2009, a securities class action lawsuit, entitled Glaser v. The9 Ltd. et al., Case No. 09-Civ-8904 was filed in the United States District Court for the Southern District of New York against us, in connection with the non-renewal of the WoW license agreement with Blizzard Entertainment, Inc. The plaintiffs in this case allege that the defendants misrepresented or failed to make material disclosures regarding the likelihood that we would be renewing the WoW license agreement with Blizzard Entertainment, Inc. The plaintiffs allege federal securities law violations and seek unspecified damages. On November 4, 2009, an additional securities class action lawsuit, entitled O. Dea v. The9 Ltd. et al., Case No. 09-Civ-9166 was filed in the United States District Court for the Southern District of New York against the same defendants with substantially the same allegations. The court consolidated these complaints into a single action on February 2, 2010, and the consolidated complaint was filed on March 19, 2010. As of the date of the filing of this annual report, we plan on filing a motion to dismiss the consolidated complaint, which is currently due on May 3, 2010. The plaintiffs must file their opposition to the motion to dismiss no later than June 17, 2010. We plan on filing a reply to their opposition, which will be due 30 days from the service of their response.

We believe that the plaintiffs' allegations have no merit and we intend to vigorously defend against the lawsuits. However, defending these lawsuits could be time-consuming and costly and could divert the attention of our senior management. We cannot predict the result of the lawsuit. An unfavorable resolution of these lawsuits or any future allegations, lawsuits or proceedings could materially and adversely affect our results of operations and financial condition and the market prices of our ADSs.

Illegal game servers, unauthorized character enhancements and other infringements of our intellectual property rights, as well as theft of in-game goods, could harm our business and reputation and materially and adversely affect our results of operation.

With the increase in the number of online game players in China, we have faced the risks of illegal game servers, unauthorized character enhancements and other infringements of our intellectual property rights as well as the risk of theft of in-game goods purchased by our customers. Our historical results of operations were materially and adversely affected by illegal game servers. Although we have adopted a number of measures to address illegal server usage, misappropriation of our game server installation software and the establishment of illegal game servers could harm our business and reputation and materially and adversely affect our results of operations.

From time to time, we have detected a number of players who have gained an unfair advantage by installing cheating tools that facilitate character progression. In response to these activities, we have expanded our customer service team dedicated to detecting unauthorized character enhancements. We have installed software patches designed to prevent unauthorized modifications to our execution files. However, we cannot assure you that we will be able to identify and eliminate new illegal game servers, unauthorized character enhancements or other infringements of our intellectual property rights in a timely manner, or at all. The deletion of unauthorized character enhancements requires the affected players to restart with a new character from the starting level, and may result in some of these players ceasing to play the game altogether. In addition, any of our new games may be affected by similar or other infringement of our intellectual property rights. If we are unable to eliminate illegal servers, unauthorized character enhancements or suffer other infringement of our intellectual property rights, our players' perception of the reliability of our games may be negatively impacted, which may reduce the number of players using our games, shorten the life span of our games or adversely affect our results of operations.

The recent global recession and the challenges the Chinese economy faces as a result could adversely affect the demand for our games and our results of operations.

We rely on the spending of our game players for our revenues, which depend on the players' level of disposable income, perceived future earnings capabilities and willingness to spend. The global recession in recent years is characterized by a general slowdown of economic growth, higher unemployment rates and reduced demand for goods and services. It is difficult to predict how long these conditions will persist and when, how fast and where recoveries will take place. The Chinese economy also faces challenges. The stimulus plans and other measures implemented by

the Chinese government in response to the global economic crisis may not work effectively or quickly enough to maintain economic growth in China or avert an economic downturn. If economic growth slows or an economic downturn occurs, our game players may reduce their spending on playing our games due to uncertain economic conditions and our business may be adversely affected.

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We face the risks of changing consumer preferences and uncertainty about market acceptance of our new products.

The online game industry is a relatively new and evolving industry in China. The level of demand and market acceptance of our online games is subject to a high degree of uncertainty. Our future operating results will depend on numerous factors beyond our control. These factors include:

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

Our ability to plan for product development and distribution and promotional activities will be significantly affected by our ability to anticipate and adapt to relatively rapid changes in consumer tastes and preferences. Currently, one of the most popular types of online games in China is the MMORPG. However, there is no assurance that MMORPGs will continue to be popular in China or that their popularity will not be surpassed by new and different types of online or other games in the future. A decline in the popularity of online games in general or the MMORPGs that we operate will likely adversely affect our business and prospects.

In addition, we expect that as we introduce new MMORPGs, a certain portion of our existing customers will switch to the new games. If this transfer of players from our existing games exceeds our expectations, we may have to adjust our marketing, pricing and other business plans and, as a result, our growth and profitability could be materially and adversely affected.

Future acquisitions may have an adverse effect on our ability to manage our business.

Selective acquisitions form a part of our strategy to further expand our business. We believe that integration of a new company's operations and personnel into ours will require significant attention of our management. The diversion of our management's attention away from our business and any difficulties encountered in the integration process could have an adverse effect on our ability to manage our business.

We intend to selectively acquire companies, technologies and personnel that are complementary to our existing business. Our ability to grow through future acquisitions, investments or organic means will depend on the availability of suitable acquisition and investment candidates at an acceptable cost, our ability to compete effectively to attract these candidates, and the availability of financing to complete larger acquisitions. We may face significant competition in acquiring new businesses or companies, which may hinder the execution of our growth strategy. Future acquisitions or investments could result in a potential dilutive issuance of equity securities or the incurrence of debt, contingent liabilities or amortization expenses related to goodwill and other intangible assets, each of which could adversely affect our financial condition and results of operations. The benefits of an acquisition or investment may also take considerable time to develop and we cannot be certain that any particular acquisition or investment will produce its intended benefits. Future acquisitions would also expose us to potential risks, including risks associated with the assimilation of new operations, technologies and personnel, unforeseen or hidden liabilities, the diversion of resources from our existing businesses, sites and technologies, the inability to generate sufficient revenue to offset the costs and expenses of acquisitions, and potential loss of, or harm to, our relationships with employees, customers, licensors and other suppliers as a result of the integration of new businesses.

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Future equity investments may have an adverse effect on our ability to manage our business.

Selective equity investments form a part of our strategy to further expand our business. To date, we have acquired equity interests in various online game developers, game studios and operators. Equity investments create a unique problem in that we are often limited in our ability to manage the products and strategies of the companies in which we invest. The diversion of our management's attention away from our business and any difficulties encountered in managing our interests in the respective investees could have an adverse effect on our ability to manage our business. In addition, we may not recover our equity investments if the companies in which we invest do not perform well, which could materially and adversely affect our results of operations.

Undetected programming errors or flaws in our games could harm our reputation or decrease market acceptance of our games, which would materially and adversely affect our results of operations.

Our games may contain errors or flaws, which may only be discovered after their release, particularly as we launch new games or introduce new features to existing games under tight time constraints. If our games contain programming errors or other flaws, our customers may be less inclined to continue or resume playing our games or recommend our games to other potential customers, and may switch to our competitors' games. Undetected programming errors and game defects can disrupt our operations, adversely affect the gaming experience of our users, harm our reputation, cause our customers to stop playing our games, divert our resources and delay market acceptance of our games, any of which could materially and adversely affect our results of operations.

We may not be able to prevent others from infringing upon our intellectual property rights, which may harm our business and expose us to litigation.

We regard our proprietary software, domain names, trade names, trademarks and similar intellectual properties as critical to our success. Intellectual property rights and confidentiality protection in China may not be as effective as in the United States or other countries. Monitoring and preventing the unauthorized use of proprietary technology is difficult and expensive. The steps we have taken may be inadequate to prevent the misappropriation of our proprietary technology. Any misappropriation could have a negative effect on our business and operating results. We may need to resort to court proceedings to enforce our intellectual property rights in the future. Litigation relating to our intellectual property might result in substantial costs and diversion of resources and management attention away from our business. See [Risks Related to Doing Business in China](#) – Uncertainties with respect to the PRC legal system could adversely affect us.

We may need additional financing and we may not be able to obtain it on terms acceptable to us, or at all.

We believe that our current cash and cash equivalents and cash flow from operations will be sufficient to meet our anticipated cash needs for the foreseeable future. We may, however, require additional cash resources due to changes in business conditions or other future developments, including any investments or acquisitions we may decide to pursue. We have made significant financial commitments under the license agreements with the licensors of the MMORPGs we operate. If our resources are insufficient to satisfy our cash requirements, we may seek additional financing in the form of additional sales of our shares, the issuance of debt securities or through obtaining a credit facility. These forms of financing may result in dilution to our shareholders or increased debt service obligations, and could result in operating and financing covenants that would restrict our operations. We cannot assure you that any such future financing will be available to us in amounts or on terms acceptable to us, if at all.

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Our sale of a significant number of equity shares to third parties may have an adverse effect on our ability to manage our business, and subsequent sales of large shareholdings by third parties may impact our share price.

In May 2007, we sold a 15% interest in our ordinary shares to EA International (Studio and Publishing) Ltd. We believe that our current cash and cash equivalents and cash flow from operations will be sufficient to meet our anticipated cash needs for the foreseeable future. We may, however, require additional cash resources due to changes in business conditions or other future developments, including any investments or acquisitions we may decide to pursue. The sale of a significant number of equity shares to a third party may have an adverse impact on our ability to manage our business, and the subsequent sale of a large equity shareholding by such a third party may impact our share price.

Any failure to maintain a stable and efficient distribution network could materially and adversely affect our business and results of operations. In addition, our dependency on one national distributor to sell our online game points could have a material adverse effect on our business.

Online payment systems in China are at an early stage of development and are not as widely available or acceptable to consumers in China as in the United States and other developed countries. See Risk Related to Doing Business in China The laws and regulations governing the online game industry in China are developing and subject to future changes. If we fail to obtain or maintain all applicable permits and approvals, our business and operations could be materially and adversely affected. We rely on a network of distributors throughout China for sales of our online game services to our customers. As a result, a substantial portion of our sales are carried out via a distribution network composed of third-party distributors. Our national distributor sells its prepaid cards to over 20,000 local distributors and Internet cafés throughout China, which in turn sell the cards to end users. End users can purchase our online game points with the prepaid cards. Currently, Beijing HuiyuanNet Technology., Ltd. is our sole national distributor. We do not have long-term agreements with our distributor. A delay or failure by our distributor to successfully market these products may decrease our revenues and competitive advantage. We cannot assure you that we will continue to maintain favorable relationships with our distributor. If we fail to maintain a stable and efficient distribution network, our business and results of operations could be materially and adversely affected.

We rely on services from third parties to carry out our businesses and to deliver our online game points to end users, and if there is any interruption or deterioration in the quality of these services, our end users may cease to use our products and services.

We rely on distributors throughout China to sell our online game points for our games. We also rely on third-party licenses for some of the software underlying our technology platform, as well as on China Telecom's Internet data centers to host our servers. See Item 4. Information on the Company B. Business Overview Pricing, Distribution and Marketing. Any interruption in our ability to obtain the services of these or other third parties or a deterioration in their performance could impair the timeliness and quality of our services. Furthermore, if our arrangements with any of these third parties are terminated or modified against our interest, we may not be able to find alternative channels of distribution on a timely basis or on terms favorable to us. If any of these events occur, our end users may cease using our products and services.

Unexpected network interruptions caused by system failures or other internal or external factors may lead to user attrition, revenue reductions and may harm our reputation.

Any failure to maintain the satisfactory performance, reliability, security and availability of our network infrastructure may cause significant harm to our reputation and our ability to attract and maintain users. The system hardware for our operations is located in several cities in China. We maintain backup system hardware in Shanghai, Shenzhen, Chengdu, Nanjing, Qingdao, Xuzhou and Shijiazhuang. We also run our back-end infrastructure in Shanghai, Shenzhen, Chengdu, Nanjing, Qingdao, Xuzhou and Shijiazhuang. Server interruptions, breakdowns or system failures in the cities where we maintain our servers and system hardware, including failures that may be attributable to sustained power shutdowns, or other events within or outside our control that could result in a sustained shutdown of all or a material portion of our services, could adversely impact our ability to service our users.

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Our network systems are also vulnerable to damage from computer viruses, fire, flood, power loss, telecommunications failures, computer hacking and similar events. We maintain property insurance policies covering our servers, but do not have business interruption insurance.

Our business may be harmed if our technology becomes obsolete or if our system infrastructure fails to operate effectively.

The online game industry is subject to rapid technological change. We need to anticipate the emergence of new technologies and games, assess their acceptance and make appropriate investments. If we are unable to do so, new technologies in online game programming or operations could render our games obsolete or unattractive.

We use our internally developed Pass9 system and other software systems that support nearly all aspects of our billing and payment transactions. Our business may be harmed if we are unable to upgrade our systems fast enough to accommodate future traffic levels, avoid obsolescence or successfully integrate any newly developed or acquired technology with our existing systems. Capacity constraints could cause unanticipated system disruptions and slower response times, affecting data transmission and game play. These factors could, among other things, cause us to lose existing or potential customers and existing or potential game development partners.

Our results of operations may be materially and adversely affected if our licensors cannot prevail on future intellectual property rights claims brought against them by third parties.

We expect to derive a considerable amount of our revenues and profits from our licensed online games in the near term, though we aim to derive more revenues from our proprietary games in the future. Any of our licensors may be subject to intellectual property rights claims with respect to the online game or games it has licensed to us. If any of our licensors cannot prevail on the intellectual property rights claims brought against it, we would lose our license from such licensor and may not be able to obtain the license from the legitimate owner of the game, and our results of operations could be materially and adversely affected.

We have been and may be subject to future intellectual property rights claims or other claims, which could result in substantial costs and diversion of our financial and management resources away from our business.

There is no assurance that our online games or other content posted on our websites do not or will not infringe upon patents, valid copyrights or other intellectual property rights held by third parties. We may be subject to legal proceedings and claims from time to time relating to the intellectual property of others. In addition, some of our employees were previously employed at other companies, including our current and potential competitors. We also intend to hire additional personnel to expand our product development and technical support teams. To the extent these employees have been involved in research at our company similar to research in which they have been involved at their former employers, we may become subject to claims that such employees have used or disclosed trade secrets or other proprietary information of their former employers. In addition, our competitors may file lawsuits against us in order to gain an unfair competitive advantage over us. In February 2010, Beijing Superior Court issued a judgment against us in a lawsuit filed by Beijing Founder Electronics Co., Ltd., which ruled that WoW client installation packages sold by us in 2007 contained fonts that infringe Beijing Founder Electronics Co., Ltd.'s intellectual property rights. Based on the judgment, we are required to compensate Beijing Founder Electronics Co., Ltd. an aggregate amount of RMB1,570,000 (US\$230,006). As the date of this annual report, we have appealed the judgment and the case is pending. If any such claim arises in the future, litigation or other dispute resolution proceedings may be necessary to retain our ability to offer our current and future games, which could result in substantial costs and diversion of our financial and management resources. Furthermore, if we are found to have violated the intellectual property rights of others, we may be enjoined from using such intellectual property, incur additional costs to license or develop alternative games and be forced to pay fines and damages, each of which may materially and adversely affect our business and results of operations.

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We experience fluctuations in quarterly operating results.

Our quarterly operating results have fluctuated in the past and will likely fluctuate in the future. These fluctuations in operating results depend on a variety of factors, including the timing of new game launches and the expiration of existing game licenses. For example, the expiration of the WoW contract in June 2009 led to a significant decrease in our revenues. Other factors include the demand for our products and the products of our competitors, the level of usage of illegal game servers, the level of usage of the Internet, the size and rate of growth of the online game market, development and promotional expenses related to the introduction of new products, network interruptions and other system problems and the outbreak of contagious diseases such as avian flu or swine flu. In addition, because our game software is susceptible to unauthorized character enhancements, we may periodically delete characters that are enhanced with unauthorized modifications. This has caused some affected customers to stop playing the respective game, which, in the aggregate, may cause our operating results to fluctuate.

To a significant degree, our operating expenses are based on planned expenditures and our expectations regarding prospective customer usage. Failure to meet our expectations could disproportionately and adversely affect our operating results in any given quarter. As a result, we believe that period-to-period comparisons of operating results are not necessarily indicative of our future results.

Our business depends substantially on the continuing efforts of our senior executives, and our business may be severely disrupted if we lose their services.

Our future success depends heavily upon the continued services of our senior executives. We rely on their expertise in business operations, technology support and sales and marketing and on their relationships with our shareholders and distributors. We do not maintain key-man life insurance for any of our key executives. If one or more of our key executives are unable or unwilling to continue in their present positions, we may not be able to replace them easily or at all. As a result, our business may be severely disrupted, our financial condition and results of operations may be materially and adversely affected, and we may incur additional expense to recruit and train personnel.

Each of our executive officers has entered into an employment agreement with us, which contain confidentiality and non-competition provisions. If any disputes arise between our executive officers and us, we cannot assure you the extent to which any of these agreements could be enforced in China, where these executive officers reside and hold most of their assets, in light of uncertainties with the PRC legal system. See Risks Related to Doing Business in China Uncertainties with respect to the PRC legal system could adversely affect us.

If we are unable to attract, train and retain key individuals and highly skilled employees, our business may be adversely affected.

If our business expands, we will need to hire and retain additional qualified employees, including skilled and experienced online game developers. Since our industry is characterized by high demand and intense competition for talent, we may need to offer higher compensation and other benefits in order to retain key personnel in the future. We cannot assure you that we will be able to attract or retain the qualified game developers or other key personnel that we will need to achieve our business objectives.

PRC laws and regulations restrict foreign ownership of Internet content provision, Internet culture operation and Internet publishing licenses, and substantial uncertainties exist with respect to the application and implementation of PRC laws and regulations.

We are a Cayman Islands company and, as such, we are classified as a foreign enterprise under PRC laws. Various regulations in China currently restrict foreign or foreign-owned entities from holding certain licenses required in China to provide online games over the Internet, including Internet content provision, or ICP, Internet culture operation and Internet publishing licenses. In light of such restrictions, we rely on Shanghai IT to hold and maintain the licenses necessary for the operation of our online games in China. Shanghai IT is a PRC company owned by Jun Zhu and Yong Wang, who are our chief executive officer and vice president, respectively.

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In July 2006, the Ministry of Information Industry (which has subsequently been reorganized as the Ministry of Industry and Information Technology), or MIIT, issued a notice, or the New MII Notice, which prohibits ICP license holders from leasing, transferring or selling a telecommunications business operating license to foreign investors in any form, or providing resources, sites or facilities to any foreign investors for their illegal operation of a telecommunications business in China. The notice also requires that ICP license holders and their shareholders directly own the domain names and trademarks used by such ICP license holders in their daily operations. The notice further requires each ICP license holder to have the necessary facilities for its approved business operations and to maintain such facilities in the regions covered by its license. In addition, all value-added telecommunication service providers are required to maintain network and information security in accordance with the standards set forth under relevant PRC regulations. The local authorities in charge of telecommunications services are required to ensure that existing ICP license holders will conduct a self-assessment of their compliance with the New MII Notice and to submit status reports to the MIIT before November 1, 2006. Since the New MII Notice was issued, we have transferred to Shanghai IT almost all of the domain names used in its daily operations and certain trademarks used in its daily operations, as required under the New MII Notice. All relevant transfers have been completed and relevant approvals have been obtained.

In September 2009, the General Administration of Press and Publication (GAPP) further promulgated the Circular Regarding the Implementation of the Department Reorganization Regulation by State Council and Relevant Interpretation by State Commission Office for Public Sector Reform to Further Strengthen the Administration of Pre-approval on Online Games and Approval on Import Online Games, or the GAPP Circular, which provides that foreign investors shall not control and participate in PRC online game operation businesses indirectly or in a disguised manner by establishing joint venture companies or entering into relevant agreements with, or by providing technical supports to, such PRC online game operation companies, or by inputting the users' registration, account management, game cards consumption directly into the interconnected gaming platform or fighting platform controlled or owned by the foreign investor. It is not yet clear how this GAPP Circular will be implemented.

If we or Shanghai IT are found to be in violation of any existing or future PRC laws or regulations, including the New MII Notice and the GAPP Circular, the relevant governmental authorities, according to the nature of the violation, would have broad discretion to adopt one or more of the following measures against us, including levying fines, confiscating our income or the income of Shanghai IT, revoking our business licenses or the business license and/or other licenses of Shanghai IT, requiring us and Shanghai IT to restructure our ownership structure or operations, and requiring us or Shanghai IT to discontinue any portion or all of our operations related to online games. Any of these actions could cause significant disruption to our business operations and may materially and adversely affect our business and financial condition and results of operations.

Subject to the interpretation and implementation of the GAPP Circular, the ownership structure and the business operation models of our PRC subsidiaries and consolidated affiliated entities comply with all applicable PRC laws, rules and regulations, and no consent, approval or license is required under any of the existing laws and regulations of China for their ownership structure and business operation models except for those which we have already obtained or which would not have a material adverse effect on our business or operations as a whole. There are, however, substantial uncertainties regarding the interpretation and application of current or future PRC laws and regulations. Accordingly, we cannot assure you that PRC government authorities will ultimately take a view that is consistent with the opinion of our PRC legal counsel.

We could also face material and adverse tax consequences if the PRC tax authorities determine that our contractual arrangements with Shanghai IT were not made on reasonable commercial terms or otherwise. If this were to occur, they may adjust our income and expenses for PRC tax purposes in the form of a transfer pricing adjustment. A transfer pricing adjustment could result in a reduction, for PRC tax purposes, of costs and expenses recorded by Shanghai IT, which could adversely affect us by: (i) increasing Shanghai IT's tax liability without reducing our PRC subsidiaries' tax liability, which could further result in late payment fees and other penalties to Shanghai IT for underpaid taxes; or (ii) limiting Shanghai IT's ability to maintain preferential tax treatments and other financial incentives.

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We may not be able to get approval for renewing our current foreign games, or for licensing new foreign games, if the PRC regulatory authorities promote a policy of domestic online game development and tighten approval criteria for online game imports.

Our business depends heavily on licensing and operating foreign games and will continue to do so in the near future. Since 2004, relevant government authorities have promulgated several circulars, according to which the development of domestically developed online games will be strategically supported by the PRC government. In July 2005, MIIT and the Ministry of Culture issued the Opinion on Development and Management of Online Games, or the Opinion. The Opinion provided that domestic software development companies, internet service providers and content providers will be encouraged, guided and supported to develop and promote self-developed and owned online games which can take up a leading position in the domestic market and expand into the international market. The government will also encourage the development of derivative products to domestic online games. In support of this policy, GAPP may tighten approval criteria for online game imports in an effort to protect the development of domestic online game enterprises, as well as to limit the influence of foreign culture on Chinese youth. If GAPP implements such rules and policies, we may not be able to get approval for renewing our current foreign game licenses or for licensing new foreign games, and our revenue and profitability may decline.

We depend on Shanghai IT to hold certain operating licenses. If Shanghai IT violates our contractual arrangements with it, our business could be disrupted and our reputation may be harmed.

Because the PRC government restricts our ownership of Internet content provision, Internet culture operation and Internet publishing businesses in China, we depend on Shanghai IT, in which we have no ownership interest, to hold and maintain certain licenses necessary for our business operations. Our relationship with Shanghai IT is governed by a series of contractual arrangements that are intended to provide us with effective control over these entities, but these contractual arrangements may not be as effective in providing control as direct ownership of these businesses. For example, Shanghai IT could violate its contractual arrangements with us, go bankrupt, suffer problems in its business or otherwise become unable to perform its contracts with us and, as a result, we may lose the licenses required for our online game operations and our reputation and business could be harmed.

The principal shareholders of Shanghai IT have potential conflicts of interest with us, which may adversely affect our business.

Our chief executive officer, Jun Zhu, and our vice president, Yong Wang, are also the principal shareholders of Shanghai IT. Thus, conflicts of interest between their duties to our company and Shanghai IT may arise. We cannot assure you that when conflicts of interest arise, these persons will act completely in our interests or that conflicts of interests will be resolved in our favor. In addition, these persons could violate their non-competition or employment agreements with us or their legal duties by diverting business opportunities from us to others. In any such event, we would have to rely on the PRC legal system to enforce these agreements. Any legal proceeding could result in the disruption of our business, diversion of our resources and the incurrence of substantial costs. See Risks Related to Doing Business in China Uncertainties with respect to the PRC legal system could adversely affect us.

Our subsidiaries in China are subject to restrictions on paying dividends or making other payments.

Current PRC regulations restrict our subsidiaries in China from paying dividends in the following two principal aspects: (i) our subsidiaries in China are only permitted to pay dividends out of their respective after-tax profits, if any, determined in accordance with PRC accounting standards and regulations, and (ii) these entities are required to allocate at least 10% of their respective after-tax profits each year, if any, to fund statutory reserve funds until the cumulative total of the allocated reserves reaches 50% of registered capital, and a portion of their respective after-tax profits to their staff welfare and bonus reserve funds as determined by their respective board of directors or shareholders. These reserves are not distributable as dividends. See Item 4. Information on the Company B. Business Overview Government regulations. Further, if these entities incur debt on their behalf in the future, the instruments governing such debt may restrict their ability to pay dividends or make other payments. Our inability to receive dividends or other payments from our PRC subsidiaries may adversely affect our ability to continue to grow our business and make cash or other distributions to the holders of our ordinary shares and ADSs. In addition, failure to comply with relevant State Administration of Foreign Exchange, or SAFE, regulations may restrict the ability of our subsidiaries to make dividend payments to us. See Risks Related to Doing Business in China PRC regulations

relating to the establishment of offshore special purpose companies by PRC residents may subject our PRC resident shareholders or us to penalties and fines, and limit our ability to inject capital into our PRC subsidiaries, limit our subsidiaries' ability to increase their registered capital, distribute profits to us, or otherwise adversely affect us.

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We have incurred losses starting from the expiration of the license of WoW. We may incur losses in the future and may not maintain profitability.

We incurred a net loss of RMB409.9 million (US\$60.1 million) in the year ended December 31, 2009 due to the non-renewal of the WoW license agreement, and we may continue to incur losses in the future. Even though we had gross profit of RMB48.0 million (US\$7.0 million) in the year ended December 31, 2009, we may not be able to sustain or increase our gross profitability in the future. We may not achieve net profitability in the future.

We expect our operating expenses to increase as we expand our operations. Our ability to achieve profitability depends on the competitiveness of our products and services as well as our ability to control costs and to provide new products and services to meet the demands of our customers. Due to the numerous risks and uncertainties associated with our business, we may not be able to achieve short-term or long-term profitability or at all. If we fail to achieve profitability in the future, the market price of our ADSs could decline.

We may not be able to successfully implement our growth strategies.

Our objective is to become a leading provider and developer of multi-platform games in China. In order to achieve this objective, we are primarily focusing on both developing proprietary games and licensed games. We also plan to further enhance our game development capability and the diversity of our game portfolio and pipeline through selective game studio acquisitions. Our business strategies may involve the development and marketing of new services and products for which there are no established markets in China or in which we lack experience and expertise. As a result, we cannot assure you that we will be able to deliver new products or services on a commercially viable basis or in a timely manner, or at all, or that we will be able to successfully implement our other growth strategies. If any of these occur, our competitiveness may be harmed and our business, financial condition and results of operations may be materially and adversely affected.

We face risks related to health epidemics and other natural disasters.

Our business could be adversely affected by the effects of H1N1, or swine influenza, avian flu, severe acute respiratory syndrome, or SARS, or another epidemic or outbreak. An outbreak of swine influenza in Mexico in the summer of 2009 has spread to China and there have been confirmed cases of swine influenza in China. Any prolonged recurrence of swine influenza, avian flu, SARS or other adverse public health developments in China may have a material adverse effect on our business operations. Our operations may be impacted by a number of health-related factors, including, among other things, quarantines or closures of our offices which could severely disrupt our operations, the sickness or death of our key officers and employees and closure of Internet cafés and other public areas where people access the Internet. Any of the foregoing events or other unforeseen consequences of public health problems could adversely affect our business and results of operations. We have not adopted any written preventive measures or contingency plans to combat any future outbreak of swine influenza, avian flu, SARS or any other epidemic. In addition, other major natural disasters may also adversely affect our business by, for example, causing disruptions of the Internet network or otherwise affecting access to our games, or resulting in damages to our facilities.

We could be liable for breaches of security on our websites and fraudulent transactions by users of our websites.

Currently, a portion of our transactions are conducted through our websites. In such transactions, secure transmission of confidential information (such as customers' credit card numbers and expiration dates, personal information and billing addresses) over public networks is essential to maintain consumer confidence. Our current security measures may not be adequate to safeguard against fraudulent transactions. Security breaches could expose us to litigation and possible liability for failing to secure confidential customer information and could harm our reputation and ability to attract customers.

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Existing major shareholders have substantial control over us and could delay or prevent a change in corporate control.

Incsight Limited, or Incsight, a company wholly-owned by Jun Zhu, our chairman and chief executive officer, and Bosma Limited, the two largest shareholders of our company, currently own, in the aggregate, a significant percentage of our outstanding ordinary shares. Incsight and Bosma have entered into a voting agreement to vote together with respect to the election of our directors. See Item 6. Directors, Senior Management and Employees C. Board Practices Voting Agreement. As a result, these shareholders will continue to exert significant control over all matters requiring shareholder approval, including but not limited to, the election of directors and approval of significant corporate transactions. This voting power could delay or prevent an acquisition of our company on terms that other shareholders may desire. In addition, the rights of minority shareholders and the fiduciary obligations of directors and majority shareholders in the Cayman Islands may not be as extensive as those in the United States or elsewhere, and the ability to assert shareholder rights may be comparatively limited.

New income tax laws may increase our tax burden or the tax burden on the holders of our shares or ADSs, and tax benefits available to us may be reduced or repealed, causing the value of your investment in us to suffer.

Our subsidiaries and affiliated entities in the PRC are subject to Enterprise Income Tax, or EIT, on the taxable income as reported in their respective statutory financial statements adjusted in accordance with the Corporate Income Tax Law of the People's Republic of China, or CIT Law, which was approved by the National People's Congress on March 16, 2007. The CIT Law went into effect as of January 1, 2008, which unified the tax rate generally applicable to both domestic and foreign-invested enterprises in the PRC. Our subsidiaries and affiliated entities in the PRC are generally subject to EIT at a statutory rate of 25%. However, some subsidiaries that are located in the Pudong New District of Shanghai are currently enjoying five year transitional EIT rates, which equate to phase-in rates of 18%, 20%, 22%, 24% and 25% for the five years from 2008 to 2012 according to local practice. Our subsidiaries and affiliated entities that hold a High and New Technology Enterprise, or HNTE, qualification are subject to a 15% preferential EIT rate.

In April 2007, China The9 Interactive (Beijing) Limited (C9I Beijing) received approval from certain government authorities to be classified as a HNTE. This classification entitles C9I Beijing to enjoy an Enterprise Income Tax, or EIT, exemption for 2007, 2008 and 2009, and a 50% reduction of the statutory rate in the three years thereafter, for which the Beijing tax authorities have granted approval. In April 2008, certain government authorities announced the new implementation rules for application and assessment of HNTE. Every qualified HNTE needs to re-apply for this qualification according to the new implementation rules. C9I Beijing re-applied for the HNTE qualification and received approval from certain government authorities. Also, Shanghai IT received approval from certain government authorities to be classified as a HNTE. This approval entitles Shanghai IT to enjoy a 15% preferential EIT rate from 2008 to 2010. The HNTE qualification is valid for a term of three years after the issuance of the approval certificate, and the enterprise is required to apply for re-examination before the end of the term. We cannot assure you that our PRC subsidiaries or affiliated entities will meet these criteria and continue to be qualified as HNTEs by the tax authorities.

Moreover, unlike the tax regulations effective before 2008, which specifically exempted withholding taxes on dividends payable to non-PRC investors from foreign-invested enterprises in the PRC, the CIT Law and its implementation rules provide that a withholding income tax rate of 10% will be applicable to dividends payable by Chinese companies to non-PRC-resident enterprises unless otherwise exempted or reduced according to treaties or arrangements between the PRC central government and governments of other countries or regions. While the Tax Agreement between the PRC and Hong Kong provides dividends paid by a foreign-invested enterprise in the PRC to its corporate shareholder, which is considered a Hong Kong tax resident, will be subject to withholding tax at the rate of 5% of total dividends, this is limited to instances where the corporate shareholder directly holds at least 25% of the shares of the company that is to pay dividends for at least 12 consecutive months immediately prior to receiving the dividends and meets certain other criteria prescribed by the relevant regulations. Entitlement to a lower tax rate on dividends according to tax treaties or arrangements between the PRC central government and governments of other countries or regions is further subject to approval of the relevant tax authority.

Furthermore, the State Administration of Taxation promulgated the Notice on How to Understand and Determine the Beneficial Owners in Tax Agreement in October 2009, or Circular 601, which provides guidance for determining whether a resident of a contracting state is the beneficial owner of an item of income under China's tax treaties and tax arrangements. According to Circular 601, a beneficial owner generally must be engaged in substantive business activities. An agent or conduit company will not be regarded as a beneficial owner and, therefore, will not qualify for treaty benefits. The conduit company normally refers to a company that is set up for the purpose of avoiding or reducing taxes or transferring or accumulating profits. We cannot assure you that any dividends to be distributed by us to our non-PRC shareholders and ADS holders whose jurisdiction of incorporation has a tax treaty with China providing a different withholding arrangement will be entitled to the benefits under the relevant withholding arrangement.

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In addition, the CIT Law deems an enterprise established offshore but having its management organ in the PRC as a resident enterprise that will be subject to PRC tax at the rate of 25% on its global income. Under the Implementation Rules of the CIT Law, the term management organ is defined as an organ which has substantial and overall management and control over the manufacturing and business operation, personnel, accounting, properties and other factors. On April 22, 2009, the State Administration of Taxation further issued a notice regarding recognizing an offshore-established enterprise controlled by PRC shareholders as a resident enterprise according to its management organ. According to this notice, a foreign enterprise controlled by a PRC company or a PRC company group shall be deemed a PRC resident enterprise, if (i) the senior management and the core management departments in charge of its daily operations are mainly located and function in the PRC; (ii) its financial decisions and human resource decisions are subject to the determination or approval of persons or institutions located in the PRC; (iii) its major assets, accounting books, company seals, minutes and files of board meetings and shareholders meetings are located or kept in the PRC; and (iv) more than half of the directors or senior management with voting rights reside in the PRC. Although our offshore companies are not controlled by any PRC company or PRC company group, we cannot assure you that we will not be deemed to be a resident enterprise under the CIT Law and thus be subject to PRC enterprise income tax on our global income.

Further, foreign corporate holders of our shares or ADSs may be subject to taxation at a rate of 10% on any dividends received from us or any gains realized from the transfer of our shares or ADSs, since such income may be regarded as income from sources within the PRC.

The CIT Law empowers the PRC State Council to enact appropriate implementing rules and measures and there is no guarantee that we or our subsidiaries will be entitled to any of the preferential tax treatments. Nor can we assure you that the tax authorities will not, in the future, discontinue any of our preferential tax treatments, potentially with retroactive effect. Any significant increase in the EIT rate under the CIT Law applicable to our PRC subsidiaries and consolidated affiliated entities, including The9 Computer Technology Consulting (Shanghai) Co., Ltd. (The9 Computer), China The9 Interactive (Shanghai) Limited (C9I Shanghai), C9I Beijing, Jiu Jing Era Information Technology (Beijing) Limited (Jiu Jing), Jiu Tuo (Shanghai) Information Technology Limited (Jiu Tuo), Shanghai The9 Advertisement Co., Ltd. (Shanghai Jiucheng Advertisement) and Shanghai IT or the imposition of withholding taxes on dividends payable by our subsidiaries to us, or an EIT levy on us or any of our subsidiaries or affiliated entities registered outside the PRC, or dividends or capital gains received by our shareholders due to shares or ADSs held in us will have a material adverse impact on our results of operations and financial conditions and the value of investments in us.

Strengthened scrutiny over acquisition transactions by the PRC tax authorities may have a negative impact on our acquisition strategy.

In connection with the CIT Law, the Ministry of Finance and State Administration of Taxation jointly issued, on April 30, 2009, the Notice on Issues Concerning Process of Enterprise Income Tax in Enterprise Restructuring Business, or Circular 59. On December 10, 2009, the State Administration of Taxation issued the Notice on Strengthening the Management on Enterprise Income Tax for Non-resident Enterprises Equity Transfer, or Circular 698. Both Circular 59 and Circular 698 became effective retroactively on January 1, 2008. Under the two circulars, non-PRC-resident enterprises may be subject to income tax on capital gains generated from their transfers of equity interests in PRC resident enterprises. The PRC tax authorities have the discretion under Circular 59 and Circular 698 to make adjustments to the taxable capital gains based on the difference between the fair value of the equity interests transferred and the cost of the investment. In addition, by promulgating and implementing the circulars, the PRC tax authorities have strengthened their scrutiny over the direct or indirect transfer of equity interests in a PRC resident enterprise by a non-PRC-resident enterprise. For example, Circular 698 specifies that the PRC State Administration of Taxation is entitled to redefine the nature of an equity transfer where offshore vehicles are interposed for tax-avoidance purposes and without reasonable commercial purpose. Since we pursue acquisitions as one of our growth strategies, and have conducted and may conduct acquisitions involving complex corporate structures, the PRC tax authorities may, at their discretion, adjust the capital gains or request us to submit additional documentation for their review in connection with any of our acquisitions, thus causing us to incur additional acquisition costs.

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We have adopted a shareholders rights plan, which, together with the other anti-takeover provisions of our articles of association, could discourage a third party from acquiring us, which could limit our shareholders' opportunity to sell their shares, including ordinary shares represented by our ADSs, at a premium.

On January 8, 2009, our board of directors adopted a shareholder rights plan. Under the rights plan, one right was distributed with respect to each of our ordinary shares outstanding at the close of business on January 22, 2009. In the event a person or group, or the Acquiring Person (as defined in the plan), obtains beneficial ownership of 15% or more of our voting securities (including by acquisition of our ADSs representing ordinary shares), or enters into an acquisition transaction without the approval of our board of directors, these rights entitle the holders other than the Acquiring Person to purchase, for an exercise price of \$19.50, a number of shares with a value twice that of the exercise price.

This rights plan and the other anti-takeover provisions of our amended and restated memorandum and articles of association could have the effect of depriving our shareholders of an opportunity to sell their shares at a premium over prevailing market prices by discouraging third parties from seeking to obtain control of our company in a tender offer or similar transaction. Our existing authorized ordinary shares confer on the holders of our ordinary shares equal rights, privileges and restrictions. The shareholders have, by virtue of adoption of our third amended and restated memorandum and articles of association, authorized the issuance of shares of par value of US\$0.01 each without specifying any special rights, privileges and restrictions. Therefore, our board of directors may, without further action by our shareholders, issue ordinary shares, or issue shares of such class and attach to such shares special rights, privileges or restrictions, which may be different from those associated with our ordinary shares. Preferred shares could also be issued quickly with terms calculated to delay or prevent a change in control of our company or make removal of management more difficult. If our board of directors decides to issue ordinary shares or issue preferred shares, the price of our ADSs may fall and the voting and other rights of the holders of our ordinary shares and ADSs may be materially and adversely affected.

We have limited business insurance coverage in China.

The insurance industry in China is still at an early stage of development. Insurance companies in China offer limited business insurance products. As a result, we do not have any business liability or disruption insurance coverage for our operations in China. Any business disruption, litigation or natural disaster might result in our incurring substantial costs and the diversion of our resources.

Some of our subsidiaries and an affiliated entity in China engaged in certain business activities beyond the authorized scope of their respective licenses, and if they are subject to administrative penalties or fines, our operating results may be adversely affected.

Some of our subsidiaries and an affiliated entity in China engaged in business activities that were not within the authorized scope of their respective licenses. For example, in 2008, The9 Computer was engaged in the distribution of WoW-related accessories, souvenirs and other merchandise. The sales that year related to such merchandise were approximately RMB0.1 million. The distribution of such merchandise, however, was not within the authorized scope of The9 Computer's business license. Shanghai IT's current ICP license was issued on May 15, 2007, and is effective until June 15, 2010. Shanghai IT did not submit a specific application, nor obtain approval for, the license for bulletin board services (BBS). In the past, Shanghai IT's main business was a virtual community, and now it is online games. BBS platforms are mainly used for communications among players and do not affect the operations of Shanghai IT. BBS platforms permit the sharing or exchange of messages and files on the network. Most of our BBS platforms are devoted to particular subjects, such as an individual MMORPG, and players can discuss game subjects and strategy. While these companies are in the process of obtaining relevant licenses, the relevant PRC authorities have the authority to impose administrative fines or other penalties for their violations, which may in turn adversely affect our operating results.

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Failure to achieve and maintain effective internal controls could have a material adverse effect on our business, results of operations and the trading price of our ADSs.

We are subject to reporting obligations under the U.S. securities laws. The Securities and Exchange Commission, or the SEC, as required by Section 404 of the Sarbanes-Oxley Act of 2002, or SOX, has adopted rules requiring public companies to include a report of management in its annual report that contains an assessment by management of the effectiveness of such company's internal controls over financial reporting. In addition, beginning with the year ended December 31, 2007, we have been required to receive an independent registered public accounting firm's report on the effectiveness of our company's internal controls over financial reporting.

Our management has concluded that our internal controls over financial reporting are effective as of December 31, 2009. If we fail to maintain effective internal controls over financial reporting in the future, our management and our independent registered public accounting firm may not be able to conclude that we have effective internal controls over financial reporting at a reasonable assurance level. This could result in a loss of investor confidence in the reliability of our financial conditions which in turn could negatively impact the trading price of our ADSs, result in lawsuits being filed against us by our shareholders or otherwise harm our reputation. Furthermore, we have incurred and anticipate that we will continue to incur considerable costs and use significant management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes Oxley Act.

We obtained WoW playing time information from a third party and used that information in connection with our recognition of revenues from the sale of WoW playing time in China during the term of our license agreement for WoW.

From June 2005 to June 2009, substantially all of our revenues have been generated from our sale of WoW playing time in China. We obtained WoW playing time information from a third party and used that information in connection with our recognition of revenues from the sale of WoW playing time in China. We sold game playing time primarily through the sales of prepaid cards and prepaid online points to distributors, who in turn sold them to our customers who play our games. Prepaid fees received from distributors for sales of game cards and online points were recognized as revenue mainly upon the customer's actual use of game playing time. Vivendi Games, Inc. maintains the systems that recorded and tracked the time that our customers spent playing the WoW game on our behalf. We were provided with data on customers' actual usage of WoW playing time by Vivendi Games, Inc., and used that data in connection with our recognition of revenues from the sale of WoW playing time in China. We do not have direct access to the systems maintained by Vivendi Games, Inc. If Vivendi Games, Inc. suffered any data loss or miscalculated the time our customers spent playing the WoW game, our results of operations may have been adversely affected.

Risks Related to Doing Business in China

Our business may be adversely affected by public opinion and government policies in China.

Currently, most of our recurring users are young males, including students. Due to the higher degree of user loyalty to MMORPGs, easy access to PCs and Internet cafés, and lack of more appealing forms of entertainment in China, many teenagers frequently play online games. This may result in these teenagers spending less time on, or refraining from, other activities, including education and sports. Internet cafés, which are currently the most important outlets for online games, have been criticized by the general public in China as exerting a negative influence on young people. Due primarily to such adverse public reaction, some local governments in China have tightened their regulation of Internet café operations through, among other things, limiting the number of new operating licenses to be issued and further reducing the hours during which the Internet cafés are permitted to be open for business. Also, local and higher-level governmental authorities may from time to time decide to more strictly enforce the customers' age limit and other requirements relating to Internet cafés as a result of the occurrence of, and the media attention on, gang fights, arson or other incidents in or related to Internet cafés. As a significant portion of our customers access our games from Internet cafés, any restrictions placed on Internet café operations could result in a reduction of the amount of time our customers spend on our online games or a reduction or slowdown in the growth of our customer base, thus adversely affecting our business and results of operations.

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In April 2007, various governmental authorities, including the General Administration of Press and Publication, the Ministry of Industry and Information Technology, the Ministry of Education, the Ministry of Public Security, and other relevant authorities jointly issued a circular concerning the mandatory implementation of an anti-fatigue system in online games, which aims to protect the physical and psychological health of minors. This circular required all online games to incorporate an anti-fatigue system and an identity verification system, both of which have limited the amount of time that a minor or other user may continuously spend playing an online game. We have implemented such anti-fatigue and identification systems on all of our online games as required. Further strengthening of these systems, or enactment by the PRC government of any additional laws to further tighten its administration over the Internet and online games or its supervision of Internet cafés may result in less time spent by customers or fewer customers playing our online games, which may materially and adversely affect our business results and prospects for future growth.

Adverse changes in economic and political policies of the PRC government could have a material adverse effect on the overall economic growth of China, which could adversely affect our business.

We conduct substantially all of our business operations in China. As the gaming industry is highly sensitive to business and personal discretionary spending levels, it tends to decline during general economic downturns. Accordingly, our results of operations, financial condition and prospects are subject to a significant degree to economic, political and legal developments in China. China's economy differs from the economies of most developed countries in many respects, including with respect to the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth in the past 20 years, growth has been uneven across different regions and among various economic sectors of China. The PRC government has implemented various measures to encourage economic development and guide the allocation of resources. While some of these measures benefit the overall PRC economy, they may also have a negative effect on us. For example, our financial condition and results of operations may be adversely affected by government control over capital investments or changes in tax regulations that are applicable to us. As the PRC economy is increasingly intricately linked to the global economy, it is affected in various respects by downturns and recessions of major economies around the world, such as the recent financial services and economic crises of these economies. The various economic and policy measures the PRC government enacts to forestall economic downturns or shore up the PRC economy could affect our business.

The PRC economy has been transitioning from a planned economy to a more market-oriented economy. Although the PRC government has implemented measures since the late 1970s emphasizing the utilization of market forces for economic reform, the reduction of state ownership of productive assets and the establishment of improved corporate governance in business enterprises, a substantial portion of productive assets in China are still owned by the PRC government. In addition, the PRC government continues to play a significant role in regulating industry development by imposing industrial policies. The PRC government also exercises significant control over China's economic growth through the allocation of resources, controlling payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. Since late 2003, the PRC government implemented a number of measures, such as raising interest rates and bank reserve requirements to place additional limitations on the ability of commercial banks to make loans, in order to contain the growth of specific segments of China's economy that it believed to be overheating. These actions, as well as future actions and policies of the PRC government, could materially affect our liquidity and access to capital and our ability to operate our business. *The laws and regulations governing the online game industry in China are developing and subject to future changes. If we fail to obtain or maintain all applicable permits and approvals, our business and operations could be materially and adversely affected.*

The online game industry in China is highly regulated by the PRC government. Various regulatory authorities of the PRC central government, such as the State Council, the Ministry of Industry and Information Technology, the General Administration of Press and Publication, the Ministry of Culture and the Ministry of Public Security, are empowered to issue and implement regulations governing various aspects of the online games industry.

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We are required to obtain applicable permits or approvals from different regulatory authorities in order to provide online games to our customers. For example, an Internet content provider, or ICP, must obtain an ICP license in order to engage in any commercial ICP operations within China. In addition, an online games operator must also obtain a license from the Ministry of Culture and a license from the General Administration of Press and Publication in order to distribute games through the Internet. If we fail to maintain any of these required permits or approvals, we may be subject to various penalties, including fines and the discontinuation or restriction of our operations. Any such disruption in our business operations would materially and adversely affect our financial condition and results of operations.

As the online games industry is at an early stage of development in China, new laws and regulations may be adopted from time to time to require additional licenses and permits other than those we currently have, and may address new issues that arise from time to time. For example, a new rule issued in June 2009 requires existing online game operators, such as our company, to obtain additional approval from the Ministry of Culture for the issuance of virtual currencies to users for online game services within three months. As a result, substantial uncertainties exist regarding the interpretation and implementation of current and any future PRC laws and regulations applicable to the online gaming industry. However, we cannot assure you that we will be able to timely obtain any new license required in the future, or at all. While we believe that we are in compliance in all material respects with all applicable PRC laws and regulations currently in effect, we cannot assure you that we will not be found in violation of any current or future PRC laws and regulations.

Intensified government regulation of Internet cafés could limit our ability to maintain or increase our revenues and expand our customer base.

In April 2001, the PRC government began tightening its supervision of Internet cafés, closing unlicensed Internet cafés, and required those remaining open to install software to prevent access to sites deemed subversive and required web portals to sign a pledge not to host subversive sites. Furthermore, the PRC government's policy, which encourages the development of a limited number of national and regional Internet café chains and discourages the establishment of independent Internet cafés, may slow the overall growth of Internet cafés. Currently, the issuance of Internet café licenses is subject to the overall planning of the Ministry of Culture and the local governments in respect of the total number and location of Internet cafés. Since 2004, the grant of new Internet café licenses has been suspended from time to time, and was again suspended in 2007. We have not been expressly notified of any suspensions in 2009, but the PRC government maintains strict controls on the granting of new licenses. As Internet cafés are the primary venue for users to play our games, any reduction in the number, or any slowdown in the growth of, Internet cafés in China will limit our ability to maintain or increase our revenues and expand our customer base, which will in turn materially and adversely affect our business and results of operations.

Regulation and censorship of information disseminated over the Internet in China may adversely affect our business, and we may be liable for information displayed on, retrieved from, or linked to our Internet websites.

The PRC government has adopted certain regulations governing Internet access and the distribution of news and other information over the Internet. Under these regulations, Internet content providers and Internet publishers are prohibited from posting or displaying over the Internet content that, among other things, violates PRC laws and regulations, impairs the national dignity of China, or is obscene, superstitious, fraudulent or defamatory. Failure to comply with these requirements could result in the revocation of ICP and other required licenses and the closure of the concerned websites. The website operator may also be held liable for such prohibited information displayed on, retrieved from or linked to such website.

The Ministry of Culture has issued a notice reiterating the government's policies to prohibit the distribution of games with violence, terror, cruelty or other elements that are believed to have the potential effect of instigating crimes, and to prevent the influx of harmful cultural products from overseas. The notice requires, among other things, the review and prior approval of all new online games licensed from foreign game developers and related license agreements, the review of patch and updates for approved games which introduce substantial changes, and the filing of domestically developed online games. We obtained the necessary approvals from the Ministry of Culture for operating MU, WoW, SUN, GE, Joyful Journey West, or JJW, EA Sports FIFA Online 2, Atlantica, World of Fighter, JiuZhouZhanJi and Kingdom Heroes 2 Online in China, and have completed the relevant filing requirement with respect to Audition 2.

We will submit new games for the required review or filing in due course. The Ministry of Culture may find the content of our new licensed games objectionable, and we may otherwise be unable to obtain the approvals for these games in a timely manner, or at all. If this happens, we will not be able to launch our new licensed games within the expected timeframe or at all, and our business and results of operations could be materially adversely affected.

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In addition, the Ministry of Industry and Information Technology has published regulations that subject website operators to potential liability for content included on their websites and the actions of users and others using their websites, including liability for violations of PRC laws prohibiting the dissemination of content deemed to be socially destabilizing. The Ministry of Public Security has the authority to order any local Internet service provider, or ISP, to block any Internet website maintained outside China at its sole discretion. Periodically, the Ministry of Public Security has stopped the dissemination over the Internet of information which it believes to be socially destabilizing. The State Secrecy Bureau, which is directly responsible for the protection of State secrets of the PRC government, is authorized to block any website it deems to be leaking state secrets or failing to meet the relevant regulations relating to the protection of state secrets in the dissemination of online information.

As these regulations are relatively new and subject to interpretation by the relevant authorities, it may not be possible for us to determine in all cases the type of content that could result in liability for us as a website operator. In addition, we may not be able to control or restrict the content of other Internet content providers linked to or accessible through our websites, or content generated or placed on our websites by our users, despite our attempt to monitor such content. To the extent that regulatory authorities find any portion of our content objectionable, they may require us to limit or eliminate the dissemination of such information or otherwise curtail the nature of such content on our websites, which may reduce our user traffic and have a material adverse effect on our financial condition and results of operations. In addition, we may be subject to significant penalties for violations of those regulations arising from information displayed on, retrieved from or linked to our websites, including a suspension or shutdown of our operations.

Future movements in exchange rates between the U.S. dollar and the RMB may adversely affect the value of our ADSs.

We are exposed to foreign exchange risk arising from various currency exposures. Our payments to overseas game developers and a portion of our financial assets are denominated in U.S. dollars while almost all of our revenues are denominated in RMB, the legal currency in China. We have not used any forward contracts or currency borrowings to hedge our exposure to foreign currency risk. The value of the RMB against the U.S. dollar and other currencies may fluctuate and is affected by, among other things, changes in political and economic conditions and China's foreign exchange policies. On July 21, 2005, the PRC government changed its decade-old policy of pegging the value of the RMB to the U.S. dollar. Under the new policy, the RMB is permitted to fluctuate within a managed band based on market supply and demand and by reference to a basket of certain foreign currencies. This change in policy caused the Renminbi to appreciate approximately 21.5% against the U.S. dollar over the following three years. Since reaching a high against the U.S. dollar in July 2008, however, the Renminbi has traded within a narrow band against the U.S. dollar, remaining within 1.0% of its July 2008 high but never exceeding it. As a consequence, the Renminbi has fluctuated sharply since July 2008 against other freely traded currencies, in tandem with the U.S. dollar. It is difficult to predict how long the current situation may last and when and how it may change again.

Our revenues and costs are mostly denominated in RMB, while a portion of our financial assets are denominated in U.S. dollars. We rely substantially on dividends and other fees paid to us by our subsidiaries and affiliated entities in China. Any significant appreciation of RMB against the U.S. dollar may adversely affect our cash flows, revenues, earnings and financial position, and the value of, and any dividends payable on, our ADSs in U.S. dollars. For example, an appreciation of RMB against the U.S. dollar would make any new RMB denominated investments or expenditures more costly to us, to the extent that we need to convert U.S. dollars into RMB for such purposes.

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Restrictions on currency exchange in China limit our ability to utilize our revenues effectively, make dividend payments and meet our foreign currency denominated obligations.

Because substantially all of our revenues are in RMB, restrictions on currency exchange in China limit our ability to utilize revenue generated in RMB to fund our business activities outside China, make dividend payments in U.S. dollars, or obtain and remit sufficient foreign currency to satisfy our foreign currency-denominated obligations, such as paying license fees and royalty payments. The principal regulation governing foreign currency exchange in China is the Foreign Currency Administration Rules (1996), as amended. Under such rules, the RMB is freely convertible for trade and service-related foreign exchange transactions, but not for direct investment, loans or investment in securities outside China unless the prior approval of the State Administration of Foreign Exchange, or SAFE, is obtained. Although the PRC government regulations now allow greater convertibility of RMB for current account transactions, significant restrictions still remain. For example, foreign exchange transactions under our PRC subsidiaries' capital account, including principal payments in respect of foreign currency-denominated obligations, remain subject to significant foreign exchange controls and the approval of SAFE. These limitations could affect our ability to obtain foreign exchange for capital expenditures. We cannot be certain that the PRC regulatory authorities will not impose more stringent restrictions on the convertibility of the RMB, especially with respect to foreign exchange transactions. *PRC regulations relating to the establishment of offshore special purpose companies by PRC residents may subject our PRC resident shareholders or us to penalties and fines, and limit our ability to inject capital into our PRC subsidiaries, limit our subsidiaries' ability to increase their registered capital, distribute profits to us, or otherwise adversely affect us.*

On October 21, 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Reverse Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies, or Notice 75, which became effective as of November 1, 2005. According to Notice 75, prior registration with the local SAFE branch is required for PRC residents to establish or to control an offshore company for the purposes of financing that offshore company with assets or equity interests in an onshore enterprise located in the PRC. An amendment to registration or filing with the local SAFE branch by such PRC resident is also required for the injection of equity interests or assets of an onshore enterprise in the offshore company or overseas funds raised by such offshore company, or any other material change involving a change in the capital or assets of the offshore company.

Moreover, Notice 75 applies retroactively. As a result, PRC residents who have established or acquired control of offshore companies that have made onshore investments in the PRC in the past are required to complete the relevant registration procedures with the local SAFE branch by March 31, 2006. Under the relevant rules, failure to comply with the registration requirements set forth in Notice 75 or the rules implementing Notice 75 may result in restrictions being imposed on the foreign exchange activities of the relevant onshore company, including the increase of its registered capital, the payment of dividends and other distributions to its offshore parent or affiliate and the capital inflow from the offshore entity, and may also subject the relevant onshore companies and PRC residents to penalties under PRC foreign exchange administration regulations.

Since May 2007, SAFE has further issued relevant guidance to its local branches with respect to the operational process for SAFE registration, which standardized more specific and stringent supervision on the registration relating to Notice 75 and imposed obligations on onshore subsidiaries of offshore special purpose companies to coordinate with and supervise the beneficial owners of the offshore entity who are PRC residents to complete the SAFE registration process.

We have requested all of our shareholders who, based on our knowledge, are PRC residents or whose ultimate beneficial owners are PRC residents to comply with all applicable SAFE registration requirements. However, we have no control over our shareholders. The failure or inability of such relevant PRC residents to comply with SAFE registration requirements may subject us or such PRC residents to fines and legal sanctions and may also limit our ability to contribute additional capital into our PRC subsidiaries, limit our subsidiaries' ability to distribute profits or make other distributions to us, or otherwise adversely affect us.

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Uncertainties with respect to the PRC legal system could adversely affect us.

We conduct our business primarily through our subsidiaries and affiliated entities incorporated in China. These entities are generally subject to laws and regulations applicable to foreign investment in China and, in particular, laws applicable to wholly-foreign owned enterprises. In addition, we depend on Shanghai IT to honor its service agreement with us. Almost all of these agreements are governed by PRC law and disputes arising out of these agreements are expected to be decided by arbitration in China. The PRC legal system is based on written statutes. Prior court decisions may be cited for reference but have limited precedential value. Since 1979, PRC legislation and regulations have significantly enhanced the protections afforded to various forms of foreign investments in China. However, since the PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involves uncertainties, which may limit legal protections available to us. In addition, any litigation in China may be protracted and result in substantial costs and diversion of resources and management attention.

The limited use of personal computers in China and the relatively high cost of Internet access with respect to per capita gross domestic product may limit the development of the Internet in China and impede our growth.

Although the use of personal computers in China has increased in recent years, the penetration rate for personal computers in China is significantly lower than in the United States and other developed countries. Furthermore, despite a decrease in the cost of Internet access in China due to a decrease in the cost of personal computers and the introduction and expansion of broadband access, the cost of Internet access in China still remains relatively high compared to the average per capita income. The limited use of personal computers in China and the relatively high cost of Internet access may limit the growth of our business. In addition, there is no assurance that there will not be any increase in Internet access or telecommunication fees in China. If that happens, the number of our users may decrease and the growth of our user base may be materially impeded.

The continued growth of China's Internet market depends on the establishment of adequate telecommunications infrastructure.

Although private sector Internet service providers currently exist in China, almost all access to the Internet is maintained through state-owned telecommunication operators under the administrative control and regulatory supervision of China's Ministry of Industry and Information Technology. In addition, the national networks in China connect to the Internet through government-controlled international gateways. These government-controlled international gateways are the only channel through which a domestic PRC user can connect to the international Internet network. We rely on this infrastructure to provide data communications capacity primarily through local telecommunications lines. Although the government has announced plans to aggressively develop the national information infrastructure, we cannot assure you that this infrastructure will be developed as planned or at all. In addition, we will have no access to alternative networks and services, on a timely basis if at all, in the event of any infrastructure disruption or failure. The Internet infrastructure in China may not support the demands necessary for the continued growth in Internet usage.

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Risks Related to Our Shares and ADSs

We were a passive foreign investment company for the taxable year ended December 31, 2009, which could result in adverse United States federal income tax consequences to U.S. Holders of our ADSs or ordinary shares.

Based on the market price of our ADSs and the value and composition of our assets, we believe we were a passive foreign investment company, or PFIC, for U.S. federal income tax purposes for our taxable year ended December 31, 2009. In addition, it is likely that one or more of our subsidiaries were also PFICs for such year. A non-U.S. corporation will be a PFIC for any taxable year if either (1) at least 75% of its gross income for such year is passive income, or (2) at least 50% of the value of its assets (based on an average of the quarterly values of the assets) during such year is attributable to assets that produce passive income or are held for the production of passive income. We must make a separate determination after the close of each taxable year as to whether we were a PFIC for that year. Because the value of our assets for purposes of the PFIC test will generally be determined by reference to the market price of our ADSs or ordinary shares, our PFIC status will depend in large part on the market price of the ADSs or ordinary shares, which may fluctuate significantly. Because we believe we were a PFIC for the taxable year ended December 31, 2009, certain adverse U.S. federal income tax consequences could apply to U.S. Holders (as defined in Item 10. Additional Information E. Taxation United States Federal Income Taxation) of our ADSs or ordinary shares with respect to any excess distribution received from us and any gain from a sale or other disposition of the ADSs or ordinary shares. See Item 10. Additional Information E. Taxation United States Federal Income Taxation Passive Foreign Investment Company.

The future sales or issuance of a substantial number of our ADSs or ordinary shares could adversely affect the price of our ADSs.

If our shareholders sell substantial amounts of our ADSs, including those issued upon the exercise of outstanding options, in the public market, the market price of our ADSs could fall. Such sales also might make it more difficult for us to sell equity or equity-related securities in the future at a time and price that we deem appropriate. If any existing shareholder or shareholders sell a substantial amount of ordinary shares, the prevailing market price for our ADSs could be adversely affected.

In addition, we may issue additional ordinary shares or ADSs for future acquisitions. If we pay for our future acquisitions in whole or in part with additionally issued ordinary shares or ADSs, your ownership interest in our company would be diluted and this, in turn, could have a material adverse effect on the price of our ADSs.

The market price for our ADSs may be volatile.

The market price for our ADSs is likely to be highly volatile and subject to wide fluctuations in response to factors including the following:

- actual or anticipated fluctuations in our quarterly operating results;
- announcements of new games by us or our competitors;
- changes in financial estimates by securities analysts;
- price fluctuations of publicly traded securities of other China-based companies engaging in Internet-related services or other similar businesses;
- conditions in the Internet or online game industries;
- changes in the economic performance or market valuations of other Internet or online game companies;
- announcements by us or our competitors of significant acquisitions, strategic partnerships, joint ventures or capital commitments;
- fluctuations in the exchange rates between the U.S. dollar and the RMB;

addition or departure of key personnel; and

pending and potential litigation.

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In addition, the securities market has from time to time experienced significant price and volume fluctuations that are not related to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our ADSs.

You may face difficulties in protecting your interests, and our ability to protect our rights through the U.S. federal courts may be limited, because we are incorporated under Cayman Islands law.

Our corporate affairs are governed by our memorandum and articles of association and by the Companies Law (2009 Revision) and common law of the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedents in the United States. In particular, the Cayman Islands has a less developed body of securities laws as compared to the United States, and provides significantly less protection to investors. Therefore, our public shareholders may have more difficulties protecting their interests in the face of actions by our management, directors or controlling shareholders than would shareholders of a corporation incorporated in a jurisdiction in the United States. In addition, Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States. As a result, our shareholders may not be able to protect their interests if they are harmed in a manner that would otherwise enable them to sue in a United States federal court.

Your ability to bring an action against us or against our directors and officers, or to enforce a judgment against us or them, will be limited because we are incorporated in the Cayman Islands, because we conduct a substantial portion of our operations in China and because the majority of our directors and officers reside outside of the United States.

We are incorporated in the Cayman Islands, and we conduct a substantial portion of our operations through our wholly-owned subsidiaries and affiliated entities in China. Most of our directors and officers reside outside of the United States and most of the assets of those persons are located outside of 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 Cayman Islands or in China in the event that you believe that your rights have been infringed under the securities laws or otherwise. Even if you are successful in bringing an action of this kind, the laws of the Cayman Islands and of China may render you unable to enforce a judgment against our assets or the assets of our directors and officers.

You may not be able to exercise your right to vote.

As a holder of ADSs, you may instruct the depositary of our ADSs to vote the shares underlying your ADSs but only if we ask the depositary to request your instruction. Otherwise, you will not be able to exercise your right to vote unless you withdraw the shares. However, you may not know about a shareholders' meeting enough in advance to withdraw the shares. Pursuant to our amended and restated memorandum and articles of association, a shareholders' meeting may be convened by us on seven business days' notice. If we ask for your instructions, the depositary will notify you of the upcoming vote and arrange to deliver our voting materials to you. We cannot assure you that you will receive the voting materials in time to ensure that you can instruct the depositary to vote your shares. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions or for the manner of carrying out voting instructions, if any such action or nonaction is in good faith. This means that you may not be able to exercise your right to vote and there may be nothing you can do if the shares underlying your ADSs are not voted as you request.

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Your right to participate in any future rights offerings may be limited, which may cause dilution to your holdings. We may from time to time distribute rights to our shareholders, including rights to acquire our securities. However, we cannot make rights available to you in the United States unless we register the rights and the securities to which the rights relate under the Securities Act of 1933, as amended, or the Securities Act, or an exemption from the registration requirements is available. Also, under the deposit agreement, the depository bank will not make rights available to you unless the distribution to ADS holders of both the rights and any related securities are either registered under the Securities Act, or exempt from registration under the Securities Act. We are under no obligation to file a registration statement with respect to any such rights or securities or to endeavor to cause such a registration statement to be declared effective. Moreover, we may not be able to establish an exemption from registration under the Securities Act. The depository may, but is not required to, sell such undistributed rights to third parties in this situation. Accordingly, you may be unable to participate in our rights offerings and may experience dilution in your holdings.

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

The depository of our ADSs has agreed to pay to you the cash dividends or other distributions it or the custodian receives on ordinary shares or other deposited securities after deducting its fees and expenses. You will receive these distributions in proportion to the number of ordinary shares your ADSs represent. However, the depository is not responsible if it decides that it is unlawful or impractical to make a distribution available to any holders of ADSs. We have no obligation to register ADSs, ordinary shares, rights or other securities under U.S. securities laws. We also have no obligation to take any other action to permit the distribution of ADSs, ordinary shares, rights or anything else to holders of ADSs. This means that you may not receive the distribution 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 adverse effect on the value of your ADSs.

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

Your ADSs represented by the ADRs are transferable on the books of the depository. However, the depository may close its transfer books at any time or from time to time when it deems expedient in connection with the performance of its duties. In addition, the depository may refuse to deliver, transfer or register transfers of ADSs generally when our books or the books of the depository are closed, or at any time if we or the depository deem it advisable to do so because of any requirement of law or of 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**

We were incorporated in the Cayman Islands on December 22, 1999 under the name GameNow.net Limited and were renamed The9 Limited in February 2004. We formed GameNow.net (Hong Kong) Limited, or GameNow, on January 17, 2000, as a wholly-owned subsidiary. We have historically conducted our operations in large part through The9 Computer, a direct wholly-owned subsidiary of GameNow in China.

In July 2003, we and China Interactive (Singapore) Pte. Ltd., or China Interactive, a privately-held Singaporean company, formed a joint venture, C9I, to acquire an exclusive license from Vivendi Games, Inc. to localize and operate the WoW game in China. We have had effective control over C9I's management and operations since its inception. In February 2005, C9I established a wholly-owned subsidiary, C9I Shanghai, to operate WoW in China through cooperation with Shanghai IT, our affiliated entity. We initially owned 54% of C9I and through a series of subsequent transactions with China Interactive, C9I became our wholly-owned subsidiary in August 2005. Our license to operate the WoW game in China expired on June 7, 2009.

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Due to the current restrictions on foreign ownership of Internet content provision, Internet culture operation and advertising businesses in China, we rely on the following two affiliated PRC entities in holding certain licenses and approvals necessary for our business operations through a series of contractual arrangements with Shanghai IT and its shareholders:

Shanghai IT, which holds Internet content provision, Internet culture operation and Internet publishing licenses;

Shanghai Jiucheng Advertisement, whose business license permits it to conduct advertisement operations. Shanghai IT is owned by Jun Zhu, our chairman and chief executive officer and shareholder, and Yong Wang, our vice president. Shanghai Jiucheng Advertisement is a subsidiary of Shanghai IT, and was incorporated in April 2007. We do not have any ownership interest in Shanghai IT or Shanghai Jiucheng Advertisement. However, each of the individual shareholders of Shanghai IT has entered into a shareholder voting proxy agreement with us, under which each such shareholder has irrevocably granted us the power to exercise voting rights on all matters to which he is entitled to vote. Each such shareholder has also entered into a call option agreement with us, pursuant to which we and/or any other parties designated by us would be entitled to acquire all or part of the equity interests in Shanghai IT to the extent permitted by the then-effective PRC laws and regulations, for the minimum amount of consideration permissible under applicable PRC laws and regulations. From 2001 to May 2005, we extended interest-free loans in an aggregate amount of RMB23.0 million to the shareholders of Shanghai IT, solely in connection with capitalizing and increasing the registered capital of Shanghai IT. These loans are repayable upon demand. The existing shareholders of Shanghai IT, Jun Zhu and Yong Wang, have pledged all of their equity interests in Shanghai IT in favor of us under an equity pledge agreement. In the event of a breach of any term in the loan agreement or any other agreement by either Shanghai IT or its shareholders, we will be entitled to enforce our rights as a pledgee under the agreement.

Our principal executive office is located at Building No. 3, 690 Bibo Road, Zhangjiang Hi-tech Park, Pudong New Area, Shanghai 201203, People's Republic of China, and our telephone number is +86-21-5172-9999. Our registered office in the Cayman Islands is located at the offices of CARD Corporate Services Ltd, Zephyr House, Mary Street, PO Box 709 George Town, Grand Cayman. Our agent for service of process in the United States is CT Corporation System located at 111 Eighth Avenue, New York, New York 10011.

In addition to our operational headquarters in Shanghai, we currently have small branch offices in the Chinese cities of Beijing, Chengdu, Nanjing, Shenyang, Wuhan and Xi'an.

Recent Developments

Developments Relating to Our Business

WoW License Agreement

Through our subsidiary C9I and our affiliated entity Shanghai IT we operated WoW, a 3D MMORPG, in China from June 2005 to June 2009 pursuant to a license agreement with Blizzard Entertainment, Inc. This agreement, which represented approximately 91% of our total revenue in 2008 and 88% of our total revenue in 2009, expired on June 7, 2009. Accordingly, we have not had revenue derived from the ongoing operation of WoW since June 7, 2009. In the second half of 2009, net revenues attributable to the operations of non-WoW games increased by 12% compared with the first half of 2009. The increase was mainly due to the revenue contribution from EA SPORTS FIFA Online 2, Atlantica and JiuZhouZhanJi.

Table of Contents*License of Games and Proprietary Games*

As of December 31, 2009, we owned or had obtained licenses to operate the following games in mainland China:

Game	Developer/Licensors	Description	Status
SUN	Webzen, Inc.	3D MMORPG	Commercially launched in China in May 2007
GE	Hanbitsoft Inc. and IMC Games Co., Ltd.	3D MMORPG	Commercially launched in China in November 2007
JiuZhouZhanJi	The9	Web game	Commercially launched in China in April 2009
EA Sports FIFA Online 2	EA Swiss Sàrl	Casual soccer game	Commercially launched in China in May 2009
Atlantica	Ndoors Corporation	3D MMORPG	Commercially launched in China in June 2009
World of Fighter	The9	2D MMORPG	Commercially launched in China in January 2010
Audition 2	G10 Entertainment Corp.	Casual dancing game	Preparing for beta testing
Kingdom Heroes 2 Online	USERJOY Technology Co., Ltd.	3D MMORPG	In closed beta testing
ShenXianZhuan	Hangzhou Fire Rain Network Technology Co., Ltd.	2.5D MMORPG	Preparing for beta testing
Miracles: Ultimate X	The9	3D MMORPG	In development
Tiny Tribe	The9	Casual game	In development
Monster of War	The9	Casual game	In development

License of SUN from Webzen, Inc.

In December 2005, we entered into an agreement with Webzen, Inc., or Webzen, a video game developer in South Korea, pursuant to which we obtained an exclusive license from Webzen to operate SUN, a 3D MMORPG, in mainland China. SUN was commercially launched in May 2007. Our license to operate SUN will expire on May 24, 2010. We are currently in negotiation with Webzen regarding a renewal contract.

License of GE from Hanbitsoft Inc. and IMC Games Co., Ltd.

In September 2004, we entered into an agreement with Hanbitsoft Inc. and IMC Games Co., Ltd., two online game developers in South Korea, pursuant to which we obtained an exclusive license to operate GE, a 3D MMORPG, in mainland China. GE was commercially launched in November 2007. Our license to operate GE will expire on November 22, 2010. We are currently in negotiation with Hanbitsoft Inc. and IMC Games Co., Ltd. regarding a renewal contract.

License and Investment by EA Swiss Sàrl/EA International (Studio and Publishing) Ltd.

In May 2007, we obtained from EA Swiss Sàrl an exclusive license to operate the EA Sports FIFA Online 2 game in mainland China. In September 2008, we entered into an amendment to the license and distribution agreement with EA Swiss Sàrl. Through this agreement we supplemented provisions of the original license agreement pertaining to updates and upgrades to EA Sports FIFA Online 2, the payment schedule for recoupable advances and the launch schedule. The game was commercially launched in mainland China in May 2009.

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EA International (Studio and Publishing) Ltd. also made an equity investment in us of approximately US\$167.0 million in exchange for 15% of our ordinary shares in May 2007. As of December 23, 2009, EA International (Studio and Publishing) Ltd. owned approximately 12.7% of our ordinary shares.

License of Atlantica from Ndoors Corporation

In April 2008, we entered into an agreement with Ndoors Corporation, or Ndoors, pursuant to which we obtained an exclusive license from Ndoors to operate the Atlantica game, a 3D MMORPG, in mainland China. The game was commercially launched in mainland China in June 2009.

Licensing to Third-Parties of World of Fighter

In May 2009, we entered into a license agreement for World of Fighter, which entitles a game operator to operate the game in Taiwan. We also licensed World of Fighter to a game operator in Hong Kong in May 2009, giving it the right to operate the game in Hong Kong and Macau. In addition, we licensed the game to game operators in South Korea in December 2009 and in Vietnam in March 2010. The game was commercially launched in mainland China in January 2010.

License of Audition 2 from G10 Entertainment Corp. and Investment in G10 Entertainment Corp.

In May 2007, we entered into an agreement with G10 Entertainment Corp., or G10, an online game developer in South Korea, pursuant to which we obtained an exclusive license from G10 to operate Audition 2, a casual dancing game, in mainland China. We are currently preparing for beta testing of Audition 2 and continue to own the license. In April 2008, we acquired a minority stake in G10, for a cash investment of approximately US\$38.3 million.

License of Kingdom Heroes 2 Online from USERJOY Technology Co., Ltd.

In July 2009, we entered into an agreement with USERJOY Technology Co., Ltd., or USERJOY, an online game developer in Taiwan, pursuant to which we obtained an exclusive license from USERJOY to operate Kingdom Heroes 2 Online in mainland China.

License of ShenXianZhuan from Fire Rain and Investment in Fire Rain

In February 2009, we invested, through Shanghai IT, in Fire Rain Network Technology Co., Limited, or Fire Rain, and obtained a 20% equity interest. We have a call option to acquire part or all of the other 80% equity interest at a pre-determined price within 24 months from the commercial launch of the games. Pursuant to our agreement with Fire Rain, we obtained an exclusive license from Fire Rain to operate ShenXianZhuan, a 3D MMORPG, in mainland China. In January 2010, we entered into an agreement with the founders of Fire Rain to acquire an additional 5% equity interest to increase our shareholding in Fire Rain to 25%.

Development of our Proprietary Games

We developed JiuZhouZhangJi, a 2D web game, in 2008. The game was commercially launched in mainland China in April 2009.

We have been developing certain other proprietary games including Miracles: Ultimate X, a 3D MMORPG game, Tiny Tribe, a 3D casual game and Monster of War, a 3D casual game, since 2008. We have conducted beta testing for Miracles: Ultimate X and Tiny Tribe in 2009. We expect to conduct beta testing for Monster of War in 2010.

Table of Contents*Investment in Red 5*

In January 2010, we acquired 16,229,470 outstanding shares of Series A convertible preferred stock of Red 5 Studios, Inc., or Red 5, an online game developer based in the United States, for US\$1.84 million, which was fully paid in January 2010. In March 2010, we entered into an agreement with Red 5, pursuant to which we will invest a total amount of US\$18.65 million cash to purchase 23,537,119 newly-issued shares of Red 5's Series A convertible preferred stock and to retain certain Red 5's employees, of which US\$11.65 million was paid in April 2010 and the remaining US\$7.0 million will be due on the first anniversary date of the transaction closing subject to certain conditions. As a result of these transactions, we now own a majority of the outstanding shares of Red 5 on an as-converted basis.

B. Business Overview

We primarily operate MMORPGs and other games that we own or in-license in China. Since February 2005, we have launched, among others, 6 MMORPGs and 3 other games. We commercially launched WoW, an MMORPG licensed from Blizzard Entertainment, Inc., in China in June 2005 through C9I Shanghai and Shanghai IT. Since WoW's commercial launch, we had relied on the game as a major source of revenue. WoW contributed approximately 91% of our total revenue in 2008 and 88% of our total revenue in 2009. We no longer operate WoW because our license agreement with Blizzard Entertainment expired on June 7, 2009. As of the date of this annual report, we have not identified a product to replace the WoW game. If we are unable to acquire, develop or license a product to replace the WoW game, our revenues will be materially impacted in the near future. Moving forward, we will continue to operate our other licensed and proprietary games, such as EA Sports' FIFA Online 2, Atlantica, World of Fighter and JiuZhouZhanJi. We plan to focus on and devote substantial resources to our research and development efforts to develop our proprietary games. Our goal is to further expand the size and capabilities of our development team by recruiting additional talented program developers, game designers and graphic artists. We also plan to introduce new game features and improve operations infrastructure to meet evolving customer tastes and expectations. For a description of the games we licensed or operated as of December 31, 2009, see Item 4. Information on the Company A. History and Development of the Company Recent Developments Developments Relating to our Business License of Games and Proprietary Games.

We are expanding our own product development capabilities to develop a suite of proprietary online games, including MMORPGs. Because MMORPGs require a significant amount of time to master, they tend to have a high degree of user attraction, which means that users tend to spend greater amounts of time playing these games than using other Internet applications. Our proprietary game, World of Fighter, a 2D MMORPG, was commercially launched in January 2010. Our other proprietary game, JiuZhouZhanJi, a web game, was commercially launched in China in April 2009. We have also developed 3D MMORPG games including Miracles: Ultimate X, and 3D casual games including Tiny Tribe and Monster of War. We will continue to develop other new games in the future. We are vigorously pursuing additional game acquisition, development and licensing agreement opportunities.

We generated our online game service revenues through either a time-based revenue model or an item-based revenue model. We used a time-based revenue model only for WoW, under which we charged players based on the time they spent playing the game. We use the item-based revenue model for our other games under which players can play the games for free, but they are charged for purchases of in-game items, such as performance-enhancing items, clothing and accessories. As the WoW license agreement expired in June 2009, our online game operation revenues will be generated primarily through the item-based revenue model in the future. Our customers typically access our online games through PCs at home or in Internet cafés. They obtain our game playing time or in-game items primarily through purchasing our prepaid cards at various retail outlets or purchasing online points at one of the more than 100,000 Internet cafés throughout China, which have subscribed to our internally developed Pass9 system. Pass9 is a proprietary, fully integrated online membership management and payment system, which offers one-stop account management and payment services to our customers and facilitates our payment arrangements with distributors and Internet cafés.

To ensure quality customer service and seamless operations, we maintain a powerful technology platform consisting of numerous servers and network devices located in ten internet data centers throughout China.

Table of Contents**Products and Services**

We offer online games including MMORPGs and our self-developed online community game, the9 City, which we offer in cooperation with Shanghai IT. In addition to MMORPGs, we have licensed or developed casual games, which emphasize play in a single sitting. Our other products and services include game operating support, website solutions and advertisement services, SMS and sales of our Pass9 system.

MMORPGs. In a typical MMORPG, thousands of players play in the same game world at the same time. MMORPG players can select a specific character to compete with in the game with which they develop experience and enhance game attributes, which can be carried over into the next higher game levels. MMORPGs incorporate many cutting-edge technology features, including:

sophisticated 2.5D or 3D graphics which expose players to captivating screen scenes;

player upgrading system which allows players to attain higher game attributes with their characters as they develop experience and enhanced game capabilities over time; and

instant messaging system which allows players to communicate with each other during the game and form groups with other players, thereby coordinating their game skills to achieve collective objectives.

As of December 31, 2009, we owned or had exclusive licenses to operate the following MMORPGs in China:

Game	Developer/Licensor	Description	Status
SUN	Webzen, Inc.	3D MMORPG	Commercially launched in China in May 2007
GE	Hanbitsoft Inc. and IMC Games Co., Ltd.	3D MMORPG	Commercially launched in China in November 2007
Atlantica	Ndoors Corporation	3D MMORPG	Commercially launched in China in June 2009
World of Fighter	The9	2D MMORPG	Commercially launched in China in January 2010
Miracles: Ultimate X	The9	3D MMORPG	In development
Kingdom Heroes 2 Online	USERJOY Technology Co., Ltd.	3D MMORPG	In closed beta testing
ShenXianZhuan	Hangzhou Fire Rain Network Technology Co., Ltd.	2.5D MMORPG	Preparing for beta testing

Casual Games. Casual games are online games targeted at a mass audience of casual gamers, such as sports games or dancing games. As opposed to complex MMORPGs, casual games are relatively simple and allow gamers to reach a final stage quickly and play in short periods of time. We believe casual games can attract a broad range of users because of features not typically available in MMORPGs.

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As of December 31, 2009, we owned or had exclusive licenses to operate the following casual games in China:

Game	Developer/Licensors	Description	Status
JiuZhouZhanJi	The9	Web game	Commercially launched in China in April 2009
EA Sports FIFA Online 2	EA Swiss Sàrl	Casual soccer game	Commercially launched in China in May 2009
Audition 2	G10 Entertainment Corp.	Casual dancing game	Preparing for beta testing
Tiny Tribe	The9	3D casual game	In development
Monster of War	The9	3D casual game	In development

In preparation for the commercial launch of a new game, we conduct closed beta testing of the game to resolve operational matters, which is followed by open beta testing in which we allow our registered users to play without charge in open market conditions to ensure performance consistency and stability of operating systems.

Our online games offer ongoing play experience which allows our users to play the game online 24 hours a day, seven days a week. Our users can access our online games from any location with an Internet connection. Substantially all of our users in China access the game servers either from PCs at home or at Internet café outlets equipped with multiple personal computers that have Internet access. Currently, a significant portion of our users access the game through Internet cafés throughout China which sell prepaid game cards or prepaid game points to their customers. To offset the impact of the limited use of online and credit card payment systems in China, we have introduced a prepaid game playing time purchase and management system, Pass9. See Membership Management and Payment System.

Other Products and Services. Our other products and services mainly consist of our online virtual community named the9 City, our game operating support, website solutions and advertisement services, SMS service, internet protocol television services, or IPTV services, and licensing of our proprietary games to third parties.

Game Operating Support, Website Solutions and Advertisement Services. Our game operating support, website solutions and advertisement services primarily relate to providing game operating support, including payment collection and processing and other online game related technical support.

SMS. Leveraging our existing user base, we offer several different SMS products and subscription packages that enable our users to, among other things, transmit and receive SMS messages, receive password protection and other value-added services.

IPTV Services. We also contract with a Chinese mobile carrier for development and maintenance of games operated on IPTV.

Licensing of Proprietary Games. In May 2009, we entered in to a license agreement for World of Fighter, which entitles a game operator in Malaysia the right to operate the game in Taiwan. We licensed World of Fighter to a game operator in Hong Kong in May 2009, giving it the right to operate the game in Hong Kong and Macau. In addition, we licensed the game to game operators in South Korea in December 2009 and in Vietnam in March 2010.

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Membership Management and Payment System

We pioneered the establishment of Pass9 in China, an integrated membership management and payment system in early 2001, which allows us to maintain a single customer database that contains each customer's profile and payment history. Pass9 provides one-stop service to our customers, distributors and developers. Pass9 provides our customers with an integrated platform to log in, pay and use any of the fee-based products and services we offer. It also allows our distributors to sell our online points to Internet cafés, and enables Internet cafés to check the balance of their points and pay us on their customers' behalf. In addition, Pass9 provides our game development partners with a simple interface to integrate their games to our system.

Our integrated membership management and payment system also incorporates a variety of community-building features, such as chat rooms, which provide registered users a platform to interact in real-time groups or one-on-one discussions, and bulletin boards which allow registered users to post notes or inquiries and respond to other users' notes or inquiries. We believe these features encourage user congregation on our site and facilitate player interaction for the games we offer. We sold our proprietary Pass9 system to third-party companies for RMB1.9 million in 2007.

Customer Service

Since our inception, we have focused on providing excellent customer service in order to retain our existing customers as well as to attract new customers. In November 2003, we received a 9001 service quality authentication certificate from the International Organization for Standardization. We believe that we are the first online game operator in China to receive such a certificate. Our online games customers can access our customer service center via phone or e-mail at any time, or visit our visitor center in Shanghai during normal business hours.

We have in-game game masters dedicated to each of the online games that we operate. Game masters are responsible for organizing in-game events, troubleshooting and actively and continuously monitoring the online game environment. Game masters are available to respond to players' inquiries, initiate the bug reporting and removal process, as well as to identify, record and deal with players' inappropriate behavior such as cheating and fighting. We believe that our provision of game masters to monitor the gaming environment is an important element in maintaining our customer loyalty and efficiently addressing technical problems as they arise.

Purchase of In-game Items and Game Playing Time

A customer can purchase in-game items and game playing time through any of the following methods:

Prepaid Cards. A customer can buy prepaid cards at retail outlets including convenience stores, supermarkets and bookstores across China.

Prepaid Online Points. Over 100,000 Internet cafés across China have subscribed to our self-developed eSales System, which is part of our Pass9 system and enables an Internet café to buy prepaid online points from our distributors and in turn sell these same points to their customers.

Online Payment. A customer can buy in-game items and game playing time online by charging payment directly to a credit or debit card. In addition, we offer free online game playing time to our new registered customers and users of our SMS service. We have also included free game cards in our marketing materials to attract new customers. Additionally, in some instances a player may access certain online games free of charge and use prepaid online points to purchase premium in-game features.

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Pricing, Distribution and Marketing

Pricing. We determine the pricing of a game near the end of the free testing period based on several factors, including the prices of other comparable games, the technological and other features of the game, and the targeted marketing position of the game. Our prepaid game cards are offered in a variety of denominations to provide users with maximum flexibility.

Distribution. Due to the limited availability of online payment systems in China, a substantial portion of our sales are carried out via a distribution network composed of third-party distributors. We sell our in-game items and game playing time primarily through sales of our online game points to end users via Beijing HuiyuanNet Technology Co., Ltd., a national online distributor. Beijing HuiyuanNet Technology Co., Ltd. sells its prepaid cards to over 20,000 local distributors and Internet cafés throughout China, which in turn sell them to end users. End users can purchase our online game points with the prepaid cards. In addition, we also directly sell game points through our game players online accounts.

Marketing. Our overall marketing strategy is to rapidly attract new customers and increase revenues from recurring customers. The marketing programs and promotional activities that we employ to promote our games include:

Advertising and Online Promotion. We place advertisements in many game magazines and on online game sites, which are updated regularly.

Cross-Marketing. We have cross-marketing relationships with major consumer brands, technology companies and major telecom carriers. We believe that our cross-marketing relationships with well-known companies will increase the recognition of our online game brands. In 2009 our cross-marketing partners included Adidas (for EA SPORTS FIFA Online 2 marketing), Gateway (for Atlantica marketing) and SONY-Ericsson (for Atlantica marketing).

On-Site Promotion. We distribute free game-related posters, promotional prepaid cards for beginners, game-related souvenirs such as watches, pens, mouse pads, calendars and paper bags at trade shows, selected Internet cafés and computer stores.

In-Game Marketing. We conduct in-game marketing programs from time to time, including online adventures for grand prizes.

Game Development and Licensing

We believe that the online game industry in China will continue its recent pattern of developing increasingly sophisticated online games tailored to the local market. In order to remain competitive, we are focusing on developing new proprietary online games. Currently, our product development team is responsible for game design, technical development and art design. We set up The9 Development Center, or TDC, on July 4, 2008. TDC is our in-house development center of online games in China. We also plan to further enhance our game development capability and diversify our game portfolio and pipeline through selective game studio acquisitions.

Our licensing process begins with a preliminary screening, review and testing of a game, followed by a cost analysis, negotiations and ultimate licensing of a game, including all regulatory and approval processes. A team is then designated to conduct closed beta testing of the game to resolve operational matters, followed by open beta testing during which our registered users may play the game without charge in open market conditions to ensure performance consistency and stability of our operation systems. Testing generally takes three to six months, during which time we commence other marketing activities.

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Technology

We aim to build a reliable and secure technology infrastructure to fully support our operations, and we maintain separate technology networks for each of our games. Our current technology infrastructure consists of the following:

servers and network devices located in eight internet data centers throughout China as of the end of December 2009;

proprietary software, including game monitor tools, that are integrated with our websites and customer service center operations; and

hardware platform and server sites primarily consisting of Lenovo, Hewlett-Packard/Compaq, Dell and IBM servers; EMC, HP and Cisco storage systems; and H3C network gears.

We have a network operation team responsible for the stability and security of our network. The team follows server workflow to detect, record, analyze and ultimately solve problems. In addition, we frequently upgrade our game server software to ensure the stability of our operation and to reduce hacking risks.

Competition

Our major competitors include, but are not limited to, online game operators in China. These include Shanda Games Limited (which operates Legend of Mir, Actoz Soft's Legend of Mir 2 and Aion), NetEase (which operates WoW, Westward Journey Online and Fantasy Westward Journey), Changyou.com Limited (which operates Tian Long Ba Bu), Perfect World, Co. Ltd. (which operates Perfect World, Zhu Xian and Chi Bi), Giant Interactive Group (which operates ZT Online and Giant Online) and Tencent (which operates, among others, Dungeon and Fighter, Cross Fire and Xun Xian.)

Our existing and potential competitors may compete with us regarding marketing activities, quality of online games and sales and distribution networks. Some of our existing and potential competitors have significantly greater financial and marketing resources than we do. For a discussion of risks relating to competition, see Item 3. Key Information D. Risk Factors Risks Related to Our Company We may not be able to maintain our market share and profitability as we operate in a highly competitive industry and compete against many companies.

Intellectual Property

Our intellectual property rights include trademarks and domain names associated with the name the9 in China and copyright and other rights associated with our websites, technology platform, self-developed software and other aspects of our business. We regard our intellectual property rights as critical to our business. We rely on trademark and copyright law, trade secret protection, non-competition and confidentiality agreements with our employees, and license agreements with our partners, to protect our intellectual property rights. We require our employees to enter into agreements requiring them to keep confidential all information relating to our customers, methods, business and trade secrets during and after their employment with us and assign their inventions developed during their employment to us. Our employees are required to acknowledge and recognize that all inventions, trade secrets, works of authorship, developments and other processes made by them during their employment are our property. We have registered our domain names with third-party domain registration entities, and have legal rights over these domain names through Shanghai IT, our affiliated PRC entity. We conduct our business under the The9 Limited brand name and the9 logo.

Legal Proceedings

See Item 8. Financial Information A. Consolidated Statements and Other Financial Information Legal Proceedings.

Government Regulations

Current PRC laws and regulations impose substantial restrictions on foreign ownership of the online gaming and Internet content provision businesses in China. As a result, we conduct our online gaming and Internet content provision businesses in China through contractual arrangements with Shanghai IT and Shanghai The9 Advertisement Co., Ltd., our affiliated PRC entities. Shanghai IT is ultimately owned by our shareholders Jun Zhu, and Yong Wang, both of whom are PRC citizens.

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In the opinion of our PRC counsel, Fangda Partners, subject to the interpretation and implementation of the GAPP Circular, the ownership structure and the business operation models of our PRC subsidiaries and our affiliated entities comply with all applicable PRC laws, rules and regulations, and no consent, approval or license is required under any of the existing laws and regulations of China for their ownership structure and business operation models except for those which we have already obtained or which would not have a material adverse effect on our business or operations as a whole.

As the online games industry is at an early stage of development in China, new laws and regulations may be adopted from time to time to require additional licenses and permits other than those we currently have, and address new issues that arise from time to time. As a result, substantial uncertainties exist regarding the interpretation and implementation of current and any future PRC laws and regulations applicable to the online games industry. See

Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China The laws and regulations governing the online game industry in China are developing and subject to future changes. If we fail to obtain or maintain all applicable permits and approvals, our business and operations could be materially and adversely affected.

Regulations on Internet Content Provision Service, Online Gaming and Internet Publishing

Our provision of online game-related content on our websites is subject to various PRC laws and regulations relating to the telecommunications industry, Internet and online gaming, and regulated by various government authorities, including the Ministry of Industry and Information Technology, or MIIT, the Ministry of Culture, the General Administration of Press and Publication and the State Administration for Industry and Commerce. The principal PRC regulations governing the Internet content provision industry as well as online gaming services in China include:

Telecommunications Regulations (2000);

The Administrative Rules for Foreign Investments in Telecommunications Enterprises (2001), as amended in 2008;

The Administrative Measures for Telecommunications Business Operating License (2009);

The Internet Information Services Administrative Measures (2000);

The Tentative Measures for Administration of Internet Culture (2003), as amended in 2004;

The Notice on Several Issues Relating to the Implementation of The Tentative Measures for Administration of Internet Culture (2003);

The Tentative Measures for Administration of Internet Publication (2002); and

The Foreign Investment Industrial Guidance Catalogue (2007).

In July 2006, the MIIT issued a notice entitled Notice on Strengthening Management of Foreign Investment in Operating Value-Added Telecommunication Services, or the New MII Notice. The New MII Notice prohibits ICP license holders from leasing, transferring or selling a telecommunications business operating license to any foreign investors in any form, or providing any resource, sites or facilities to any foreign investors for their illegal operation of telecommunications businesses in China. The notice also requires that ICP license holders and their shareholders directly own the domain names and trademarks used by such ICP license holders in their daily operations. The notice further requires each ICP license holder to have the necessary facilities for its approved business operations and to maintain such facilities in the regions covered by its license. In addition, all the value-added telecommunication service providers are required to maintain network and information security in accordance with the standards set forth under relevant PRC regulations. The local authorities in charge of telecommunications services are required to ensure that existing ICP license holders conduct a self-assessment of their compliance with the New MII Notice and to submit status reports to the MIIT before November 1, 2006. For those which are not in compliance with the above requirements and further fail to rectify the situation, the relevant governmental authorities would have broad

discretion to adopt one or more measures against them, including but not limited to revoking their operating licenses. See Item 3. Key Information D. Risk Factors Risks Related to Our Company PRC laws and regulations restrict foreign ownership of Internet content provision, Internet culture operation and Internet publishing licenses, and substantial uncertainties exist with respect to the application and implementation of PRC laws and regulations.

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Under these regulations, a foreign investor is currently prohibited from owning more than 50% of the equity interest in a PRC entity that provides value-added telecommunications services. Internet content provision services are classified as value-added telecommunications businesses, and a commercial operator of such services must obtain a value-added telecommunications business operating license for Internet content provision, or the ICP License, from the appropriate telecommunications authorities in order to carry on any commercial Internet content provision operations in China.

With respect to the online gaming industry in China, since online games fall into the definition of Internet culture products under The Tentative Measures for Internet Culture Administration (2003), a commercial operator of online games must, in addition to obtaining the ICP License, obtain an Internet culture operation license from the appropriate culture administrative authorities for its operation of online games. Furthermore, according to The Tentative Measures for Internet Publication Administration (2002), the provision of online games is deemed an Internet publication activity. Therefore, approval from the appropriate press and publication administrative authorities as an Internet publisher or cooperation with a licensed Internet publisher is required for an online game operator to carry on its online gaming businesses in China. Furthermore, online games, regardless of whether imported or domestic, must be registered with the Ministry of Industry and Information Technology and such online games are subject to a content review and approval by or a filing with the Ministry of Culture and the General Administration of Press and Publication prior to commencement of operations in China.

The General Administration of Press and Publication and the Ministry of Industry and Information Technology jointly impose a license requirement for any company that intends to engage in Internet publishing, defined as any act by an Internet information service provider to select, edit and process content or programs and to make such content or programs publicly available on the Internet. Furthermore, the distribution of online game cards and CD-keys for online gaming programs is subject to a licensing requirement. Shanghai IT holds the license necessary to distribute electronic publications, which allows it to distribute prepaid cards and CD-Keys for the games we operate. We sell our prepaid cards and CD-Keys through third-party distributors, which are responsible for maintaining requisite licenses for distributing our prepaid cards and CD Keys in China. See Item 3. Key Information D. Risk Factors Risks Related to Our Company We rely on services from third parties to carry out our businesses and to deliver our online game points to end users, and if there is any interruption or deterioration in the quality of these services, our end users may cease to use our products and services.

On February 15, 2007, fourteen governmental authorities, including the Ministry of Culture, the MIIT, the State Administration for Industry and Commerce, and the People's Bank of China, or the PBOC, jointly issued a circular entitled *Circular for Further Strengthening the Administration of Internet Café and Online Games*. This circular gave the PBOC administrative authority over virtual currencies issued by online game operators for use by players in online games to avoid the potential impact such virtual currencies may have on the real-world financial systems. According to this circular, the volume that may be issued and the purchase of such virtual currencies must be restricted, and virtual currency must not be used for the purchase of any physical products, refunded with a premium or otherwise illegally traded. The Ministry of Culture and the Ministry of Commerce promulgated A Notice of Strengthening the Management of Virtual Currency of Online Games on June 4, 2009, which imposes more restrictions and requirements on online game operators that issue virtual currencies. According to the notice, an online game operator which issues virtual currency used for online game services shall apply for approval from the Ministry of Culture. Online game operators which have already engaged in the virtual currency issuance business, such as Shanghai IT, shall apply for such approval within three months after the promulgation of the notice. An online game operator shall further report detailed rules of issuance for virtual currencies, such as distribution scope, pricing, and terms for refunds and shall make certain periodic and supplementary filings as required by the notice. In addition, under the new rules, online game operators are prohibited from assigning game tools or virtual currency to users by way of drawing lots, random samplings or other arbitrary means in exchange for users' cash or virtual currency.

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In September 2009, the General Administration of Press and Publication (GAPP) further promulgated the Circular Regarding the Implementation of the Department Reorganization Regulation by State Council and Relevant Interpretation by State Commission Office for Public Sector Reform to Further Strengthen the Administration of Pre-approval on Online Games and Approval on Import Online Games, or the GAPP Circular, which provides that foreign investors are prohibited from making investment and engaging in online game operation services by setting up foreign-invested enterprises in China. Further, foreign investors shall not control and participate in PRC online game operation businesses indirectly or in a disguised manner by establishing joint venture companies or entering into agreements with or providing technical support to such PRC online game operation companies, or by inputting the users' registration, account management, game cards consumption directly into the interconnected gaming platform or fighting platform controlled or owned by the foreign investor. The relevant governmental authorities have broad discretion to adopt one or more of administrative measures against companies now in compliance with these measures, including revoking relevant licenses and relevant registration. See Item 3. Key Information D. Risk Factors

Risks Related to Our Company PRC laws and regulations restrict foreign ownership of Internet content provision, Internet culture operation and Internet publishing licenses, and substantial uncertainties exist with respect to the application and implementation of PRC laws and regulations.

The operation of SMS in China is classified as a value-added telecommunication business and SMS service providers shall obtain the relevant value-added telecommunication business permits.

Furthermore, the MIIT has promulgated rules requiring ICP license holders that provide online bulletin board services to register with, and obtain approval from, the relevant telecommunication authorities.

Regulations on Internet Content

The PRC government has promulgated measures relating to Internet content through a number of ministries and agencies, including the MIIT, the Ministry of Culture and the General Administration of Press and Publication. These measures specifically prohibit Internet activities, which includes the operation of online games that result in the publication of any content which is found to, among other things, propagate obscenity, gambling or violence, instigate crimes, undermine public morality or the cultural traditions of the PRC, or compromise State security or secrets. See

Item 3. Key Information D. Risks Factors Risks Related to Doing Business in China The laws and regulations governing the online game industry in China are developing and subject to future changes. If we fail to obtain or maintain all applicable permits and approvals, our business and operations could be materially and adversely affected. If an ICP license holder violates these measures, the PRC government may revoke its ICP license and shut down its websites.

In April 2007, various governmental authorities, including the General Administration of Press and Publication, the MIIT, the Ministry of Education, the Ministry of Public Security, and other relevant authorities jointly issued a circular concerning the mandatory implementation of an anti-fatigue system in online games, which was aimed at protecting the physical and psychological health of minors. This circular required all online games to incorporate an anti-fatigue system and an identity verification system, both of which have limited the amount of time that a minor or other user may continuously spend playing an online game. We have implemented such anti-fatigue and identification systems on all of our online games as required. Additional requirements for anti-fatigue and identification systems in our games, as well as the implementation of any other measures required by any new regulations the PRC government may enact to further tighten its administration of the Internet and online games, and its supervision of Internet cafés, may limit or slow down our prospects for growth, or may materially and adversely affect our business results. See

Item 3. Key Information D. Risks Factors Risks Related to Doing Business in China Our business may be adversely affected by public opinion and government policies in China.

Internet content in China is also regulated and restricted from a state security standpoint. The National People's Congress, China's national legislative body, has enacted a law that may subject to criminal punishment in China any effort to: (1) gain improper entry into a computer or system of strategic importance; (2) disseminate politically disruptive information; (3) leak state secrets; (4) spread false commercial information; or (5) infringe intellectual property rights.

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The Ministry of Public Security has promulgated measures that prohibit use of the Internet in ways which, among other things, result in a leakage of state secrets or a spread of socially destabilizing content. The Ministry of Public Security has supervision and inspection rights in this regard, and we may be subject to the jurisdiction of the local security bureaus. See Item 3. Key Information D. Risks Factors Risks Related to Doing Business in China Regulation and censorship of information disseminated over the Internet in China may adversely affect our business, and we may be liable for information displayed on, retrieved from, or linked to our Internet websites. If an ICP license holder violates these measures, the PRC government may revoke its ICP license and shut down its websites.

Regulations on Internet Café

Internet cafés are required to obtain a license from the Ministry of Culture and the State Administration for Industry and Commerce, and are subject to requirements and regulations with respect to location, size, number of computers, age limit of customers and business hours. Although we do not own or operate any Internet cafés, many Internet cafés distribute our virtual pre-paid cards. The PRC government has enacted laws to intensify its regulation and administration of Internet cafés, which are currently the primary venue for our users to play online games. Intensified government regulation of Internet cafés could restrict our ability to maintain or increase our revenues and expand our customer base. See Item 3. Key Information D. Risks Factors Risks Related to Doing Business in China Intensified government regulation of Internet cafés could limit our ability to maintain or increase our revenues and expand our customer base.

Regulations on Privacy Protection

PRC laws and regulations do not prohibit Internet content providers from collecting and analyzing personal information from their users. We require our users to accept a user agreement whereby they agree to provide certain personal information to us. PRC law prohibits Internet content providers from disclosing to any third parties any information transmitted by users through their networks unless otherwise permitted by law. If an Internet content provider violates these regulations, the Ministry of Industry and Information Technology or its local bureaus may impose penalties and the Internet content provider may be liable for damages caused to its users.

Import Regulations

Our ability to obtain licenses for online games from abroad and import them into China is regulated in several ways. We are required to register with the Ministry of Commerce any license agreement with a foreign licensor that involves an import of technologies, including online game software into China. Without that registration, we may not remit licensing fees out of China to any foreign game licensor. In addition, the Ministry of Culture requires us to submit for its content review and/or approval any online games we want to license from overseas game developers or any patch or updates for such game if it contains substantial changes. If we license and operate games without that approval, the Ministry of Culture may impose penalties on us, including revoking the Internet culture operation license required for the operation of online games in China. Also, pursuant to a jointly issued notice in July 2004, the General Administration of Press and Publication and the State Copyright Bureau require us to obtain their approval for imported online game publications. Furthermore, the State Copyright Bureau requires us to register copyright license agreements relating to imported software. Without the State Copyright Bureau registration, we cannot remit licensing fees out of China to any foreign game licensor and we are not allowed to publish or reproduce the imported game software in China.

Regulations on Intellectual Property Rights

The State Council and the State Copyright Bureau have promulgated various regulations and rules relating to the protection of software in China. Under these regulations and rules, software owners, licensees and transferees may register their rights in software with the State Copyright Bureau or its local branches and obtain software copyright registration certificates. Although such registration is not mandatory under PRC law, software owners, licensees and transferees are encouraged to go through the registration process and registered software rights may receive better protection. We have registered all of our in-house developed online games with the State Copyright Bureau.

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Regulations on Foreign Currency Exchange and Dividend Distribution

Foreign Currency Exchange. Foreign currency exchange regulation in China is primarily governed by the following rules:

Foreign Exchange Administration Rules (1996), as amended, or the Exchange Rules; and

Administration Rules of the Settlement, Sale and Payment of Foreign Exchange (1996), or the Administration Rules.

Pursuant to the Exchange Rules, the RMB is freely convertible for trade and service-related foreign exchange transactions, but not for direct investment, loans, investment in securities, or other transactions through a capital account outside China unless the prior approval of the State Administration of Foreign Exchange of the People's Republic of China is obtained. Further, foreign investment enterprises in China may purchase foreign exchange without the approval of the State Administration of Foreign Exchange of the People's Republic of China for trade and service-related foreign exchange transactions by providing commercial documents evidencing these transactions. Foreign investment enterprises that need foreign exchange for the distribution of profits to their shareholders may effect payment from their foreign exchange account or purchase and pay foreign exchange at the designated foreign exchange banks to their foreign shareholders by producing board resolutions for such profit distribution. Under the Administration Rules, based on their needs, foreign investment enterprises are permitted to open foreign exchange settlement accounts for current account receipts and payments of foreign exchange along with specialized accounts for capital account receipts and payments of foreign exchange at certain designated foreign exchange banks.

Dividend Distribution. The principal regulations governing distribution of dividends of foreign holding companies include:

The Foreign Investment Enterprise Law (1986), as amended; and

Administrative Rules under the Foreign Investment Enterprise Law (2001).

Under these regulations, foreign investment enterprises in China may pay dividends only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. In addition, foreign investment enterprises in China are required to allocate at least 10% of their respective profits each year, if any, to fund certain reserve funds until the cumulative total of the allocated reserve funds reaches 50% of an enterprise's registered capital and a portion of their respective after-tax profits to their staff welfare and bonus reserve funds as determined by their respective board of directors or shareholders. These reserves are not distributable as dividends.

Regulations on Foreign Exchange in Certain Onshore and Offshore Transactions

On October 21, 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Reverse Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies, or Notice 75, which became effective as of November 1, 2005.

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According to Notice 75:

prior to establishing or assuming control of an offshore company for the purposes of financing that offshore company with assets or equity interests in an onshore enterprise in the PRC, each PRC resident, whether a natural person or a legal entity, must complete the overseas investment foreign exchange registration procedures with the local SAFE branch;

an amendment to the registration with the local SAFE branch is required to be filed by any PRC resident that directly or indirectly holds interests in that offshore company upon either (1) the injection of equity interests or assets of an onshore enterprise in the offshore company, or (2) the completion of any overseas fundraising by such offshore company; and

an amendment to the registration with the local SAFE branch is also required to be filed by such PRC resident when there is any material change involving a change in the capital of the offshore company, such as (1) an increase or decrease in its capital, (2) a transfer or swap of shares, (3) a merger or division, (4) a long-term equity or debt investment, or (5) the creation of any security interests over the relevant assets located in China.

Moreover, Notice 75 applies retroactively. As a result, PRC residents who have established or acquired control of offshore companies that have made onshore investments in the PRC in the past are required to complete the relevant overseas investment foreign exchange registration requirements by March 31, 2006. Under the relevant rules, failure to comply with the registration procedures set forth in Notice 75 or the rules implementing Notice 75 may result in restrictions being imposed on the foreign exchange activities of the relevant onshore company, including an increase of its registered capital, the payment of dividends and other distributions to its offshore parent or affiliate and the capital inflow from the offshore entity, and may also subject the relevant onshore company and PRC residents to penalties under PRC foreign exchange administration regulations.

Since May 2007, SAFE has further issued relevant guidance to its local branches with respect to the operational process for SAFE registration, which standardized more specific and stringent supervision on the registration relating to Notice 75 and imposed obligations on onshore subsidiaries of offshore special purpose companies to coordinate with and supervise the beneficial owners of the offshore entity who are PRC residents to complete the SAFE registration process.

As a result of the uncertainties relating to the interpretation and implementation of Notice 75, we cannot predict how these regulations will affect our business operations or strategies. For example, our present or future PRC subsidiaries ability to conduct foreign exchange activities, such as remittance of dividends and foreign-currency-denominated borrowings, may be subject to compliance with such SAFE registration requirements by relevant PRC residents, over whom we have no control. In addition, we cannot assure you that any such PRC residents will be able to complete the necessary approval and registration procedures required by the SAFE regulations. We have requested that all of our shareholders whom we know are PRC residents or which have PRC residents as their ultimate beneficial owners comply with any SAFE registration requirement, but we have no control over our shareholders. Any non-compliance may adversely affect our ability to expatriate dividends or other distributions or receive capital inflow from offshore entities and may restrict our ability to implement our acquisition strategy and adversely affect our business and prospects.

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C. Organizational Structure

The following diagram illustrates our company's organizational structure, and the place of formation, ownership interest of each of our subsidiaries and affiliated entities that operate our major game platforms in China. For a listing of all of our subsidiaries and affiliated entities, see Exhibit 8.1 filed herewith.

D. Property, Plant and Equipment

Our headquarters are located on premises comprising approximately 14,000 square meters in an office building in Shanghai, China. We purchased the office building in which our headquarters are located, and lease all of our other premises from unrelated third parties. In addition, we have small branch offices in Beijing, Nanjing, Wuhan, Xi'an, Chengdu and Shenyang, China. We bought an approximately 3,000 square meter office space in Nanjing. We rent an approximately 300 square meter office for The9 Development Center near our office building in Shanghai, a 400 square meter office in Nanjing and a 1,000 square meter office in Beijing. Our equipment consists substantially of numerous servers and network devices located in eight internet data centers throughout China.

ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion of our financial condition and results of operations is based upon and should be read in conjunction with our consolidated financial statements and their related notes included in this annual report. This report contains forward-looking statements. See H. Safe Harbor. In evaluating our business, you should carefully consider the information provided under the caption Risk Factors in this annual report. We caution you that our businesses and financial performance are subject to substantial risks and uncertainties.

A. Overview

We have historically derived substantially all of our revenues through our wholly-owned subsidiary C9I and its operation of WoW in China through cooperation with Shanghai IT. WoW was commercially launched in China in June 2005. In 2007, 2008 and 2009, 92%, 91% and 88% of our total revenues, respectively, were attributable to the operation of WoW in China, including game playing time, merchandise sales and other related revenues. Our license to operate the WoW game in China expired on June 7, 2009. As a result, our revenues decreased by 55.6% from RMB1,806.1 million in 2008 to RMB802.6 million (US\$117.6 million) in 2009. As of the date of this annual report, we have not identified a product to replace the WoW game. We expect that we will depend more on our relationships with other existing game licensors, such as EA Swiss Sàrl, Webzen, Inc., G10 Entertainment Corp., Hanbitsoft Inc., Ndoors Corporation and USERJOY Technology Co., Ltd. in the near future. If we are unable to acquire, develop or license a product to replace the WoW game, our revenues will continue to be materially impacted in the near future. In addition, our license agreement with Webzen to operate SUN will expire on May 24, 2010 and our license agreement with Hanbitsoft Inc. and IMC Games Co., Ltd. to operate GE will expire on November 22, 2010. We are currently in the process of negotiating SUN and GE renewal contracts.

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To broaden our product offerings, we have obtained exclusive licenses to operate additional online games in China, including EA Sports FIFA Online 2, Atlantica, Kingdom Heroes 2 Online and Audition 2. In 2009, we commercially launched one additional MMORPG, Atlantica, one casual game, EA Sports FIFA Online 2 and one proprietary web game, JiuZhouZhanJi. In addition, one of our proprietary games, World of Fighter, a 2D MMORPG, was commercially launched in January 2010. We are also preparing for the launch of Kingdom Heroes 2 Online, Audition 2 and our other proprietary online games.

The major factors affecting our results of operations and financial condition include:

our revenue composition and sources of revenue;

our cost of services; and

our operating expenses.

Each of these factors is discussed below.

Revenue Composition and Sources of Revenue.

In 2007, 2008 and 2009, we generated substantially all of our revenues from online game services, and a minor portion of our revenues from other services. The following table sets forth the revenues generated from our online game services in China and other services, both in absolute amount and as a percentage of total revenues for the periods indicated.

	For the Year Ended December 31, 2007		For the Year Ended December 31, 2008		For the Year Ended December 31, 2009		
	RMB	%	RMB	%	RMB	US\$	%
	(in thousands except percentages)						
Revenues:							
Online game operation	1,330,977	98.6	1,800,313	99.7	795,477	116,538	99.1
Other revenues	19,152	1.4	5,817	0.3	7,152	1,048	0.9
Total revenues	1,350,129	100	1,806,130	100	802,629	117,586	100

Online Game Services. Our online game service revenues for the years before 2005 were primarily derived from sales of prepaid playing time for the9 City. Since we commercially launched WoW in China in June 2005, we have derived substantially all of our online game service revenues from sales of WoW playing time. In 2007, 2008 and 2009, revenues from our online game services amounted to RMB1,331.0 million, RMB1,800.3 million and RMB795.5 million (US\$116.5 million), respectively. The decrease in revenue in 2009 from 2008 was mainly due to revenue losses from the non-renewal of the WoW license agreement in June 2009.

We generated our online game service revenues through either time-based revenue model or item-based revenue model. We used a time-based revenue model only for WoW, under which we charged players based on the time they spend playing the game. We use an item-based revenue model for our other games under which players can play the games for free, but they are charged for purchases of in-game items, such as performance-enhancing items, clothing and accessories. As the WoW license agreement expired in June 2009, our online game operation revenues will be generated primarily through the item-based revenue model in the future.

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In the item-based revenue model, we generate online game service revenues through the sale of in-game premium features. In this model, players can access our basic games free of charge and then may use game points to purchase in-game premium features. The distribution of points to end users is typically made through sales of prepaid game cards and prepaid online points. Fees of prepaid game cards and prepaid online points are deferred when initially received. This revenue is recognized over the life of the premium features or as the premium features are consumed. Future usage patterns may differ from the historical usage patterns on which the virtual items and services consumption model is based. We will continue to monitor the operational statistics and usage patterns.

In the time-based model, we generate online game service revenues through the sale of playing time, mostly through sales of prepaid cards and prepaid online points to distributors who in turn sell them to end users. Both prepaid cards and prepaid online points provide customers with a pre-specified length of game playing time. All prepaid fees received from distributors are initially recognized as advances from customers. Prepaid fees are recognized as deferred revenue upon the customers' online registration and activation of their cards or online points, and then recognized as revenue upon the actual usage of the game playing time by end customers or when the likelihood that it will provide further online game service to those customers is remote.

Other Revenues. Prior to the commercial launch of WoW in China in June 2005, we derived a significant portion of our revenues from providing game operating support and website solutions and advertisement services, including website development and construction, hardware and software support, staff training, maintenance and advertisement. We also derived revenues from SMS services and from the sales of game-related accessories and merchandise. In recent years, these revenues were mainly divided into (i) revenue from our contracts with various Chinese mobile carriers for the transmission of short messaging services, (ii) revenue from our game operating support, website solutions and advertisement services, (iii) revenue generated from licensing our proprietary games developed by us to overseas game operators, (iv) revenue generated from our contracts with a Chinese mobile carrier for development and maintenance of games operated on IPTV and (v) revenue from sales of certain online game-related software packages and accessory merchandise. In 2007, 2008 and 2009, revenues from our other products and services amounted to RMB19.2 million, RMB5.8 million and RMB7.2 million (US\$1.0 million), respectively.

Cost of Services. Our cost of services consists of costs directly attributable to rendering our products and services, including online game royalties, payroll, depreciation, maintenance and rental of operation sites, depreciation and amortization of computer equipment and software, production costs for prepaid game cards, intangible assets amortization and other overhead expenses directly attributable to the services we provided.

Operating Expenses. Our operating expenses consist primarily of product development expenses, sales and marketing expenses, general and administrative expenses and impairment expenses.

Product Development Expenses. Our product development expenses consist primarily of compensation to our product development personnel, outsource research and development expenses, equipment and software depreciation charges and other expenses for the development of online games. Our other product development costs include costs that we have incurred to develop and maintain our websites. We expect that our product development expenses will increase in the near future as we expand our internal game development capabilities.

Sales and Marketing Expenses. Our sales and marketing expenses primarily consist of advertising and marketing expenses to promote our games and compensation to our sales and marketing personnel. Advertising expenses in the amount of RMB41.5 million, RMB23.9 million and RMB33.1 million (US\$4.8 million) for the years ended December 31, 2007, 2008 and 2009, respectively, were expensed as incurred. Marketing expenses will increase during the periods we launch our new games.

General and Administrative Expenses. Our general and administrative expenses consist primarily of compensation and travel expenses for our administrative staff, depreciation of property and equipment, entertainment expenses, provision for doubtful accounts and provision for prepayments and other current assets, administrative office expenses, as well as fees paid to professional service providers for auditing and legal services. We expect general and administrative expenses will increase with the expansion of our business.

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Impairment. Impairment charges consist of our expenses associated with the impairment of certain equipment, intangible assets and goodwill.

Recent Impairment Provisions Related to the Non-renewal of the WoW License

As a result of the non-renewal of the WoW license agreement beyond June 7, 2009, we recorded impairment and certain other charges in our consolidated financial statements for the year ended December 31, 2008 as follows:

A provision on a receivable amounting to RMB18.0 million from a customer that purchased WoW prepaid player cards from the company for distribution, as a result of the expiration of the WoW license on June 7, 2009 and, among other things, the impact on the ongoing relationship with the customer;

A RMB3.9 million provision for prepaid royalties;

A RMB22.7 million charge to increase the valuation allowance for deferred tax assets, which represented incremental income taxes as a result of non-renewal of the WoW license prior to the evaluation and recording of impairment charges as a result of the non-renewal of the WoW license;

RMB68.4 million of additional depreciation expense related to computer equipment to reflect the change to a shorter expected useful life of the underlying assets due to non-renewal of the WoW license agreement;

A RMB46.5 million provision for prepayment for equipment and a RMB8.7 million provision on advances to suppliers mainly related to a vendor which had been the primary supplier of computer servers and related computer equipment. With the non-renewal of the WoW license, we evaluated a number of factors, including the status of production of the assets underlying the advance prepayments, our ability to recover the value of the advances through the possible sale of the fixed assets upon the completion of production, the ability to utilize the servers upon completion of production, as well as our ability to recover the amounts advanced to the vendor and as a result of such assessment, and concluded that a full provision in connection with such advances and prepayments was necessary;

RMB7.0 million provisions on receivable and prepayments and other current assets in connection with Game First International Corporation, or GFD, comprising: (i) a RMB5.6 million provision on prepayments and other current assets. We assessed the impact of non-renewal of the WoW license on its ongoing relationship with GFD and the resulting collectability of this receivable, and concluded collection to be unlikely; and (ii) a RMB1.4 million provision on accounts receivable; and

A RMB1.7 million provision on inventories.

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As a result of the non-renewal of the WoW license agreement beyond June 7, 2009, we recorded impairment and certain other charges in our consolidated financial statements for the year ended December 31, 2009 as follows:

A RMB103.2 million (US\$15.1 million) provision for royalty prepayments including withholding taxes that were paid in 2009 but not consumed prior to the expiration of the WoW license on June 7, 2009;

RMB40.0 million (US\$5.9 million) of additional depreciation expense related to computer equipment to reflect the change to a shorter expected useful life of the underlying assets due to the non-renewal of the WoW license agreement;

A RMB30.2 million (US\$4.4 million) impairment for goodwill which was deemed recoverable as of December 31, 2008 based on our company's impairment test that includes the operating cash flow generated from WoW operation during the period from January 1 to June 6, 2009, but was no longer recoverable following the expiration of the WoW license on June 7, 2009; and

A RMB22.1 million (US\$3.2 million) provision for additional cost of services related to the refund of point cards, which is the difference between the face value of the point cards and the net proceeds our company received in the sales of the respective point cards.

Holding Company Structure

We are a holding company incorporated in the Cayman Islands and rely primarily on dividends and other distributions from our subsidiaries and our affiliates in China for our cash requirements. Current PRC regulations restrict our affiliated entities and subsidiaries from paying dividends in the following two principal aspects: (i) our affiliated entities and subsidiaries in China are only permitted to pay dividends out of their respective accumulated profits, if any, determined in accordance with PRC accounting standards and regulations; and (ii) these entities are required to allocate at least 10% of their respective accumulated profits each year, if any, to fund certain capital reserves until the cumulative total of the allocated reserves reach 50% of registered capital, and a portion of their respective after-tax profits to their staff welfare and bonus reserve funds as determined by their respective boards of directors. These reserves are not distributable as dividends. See Item 4. Information on the Company B. Business Overview Government Regulations. In addition, failure to comply with relevant State Administration of Foreign Exchange, or SAFE, regulations may restrict the ability of our subsidiaries to make dividend payments to us. See Item 3. Key Information D. Risk Factors Risks Related to Doing Business in China PRC regulations relating to the establishment of offshore special purpose companies by PRC residents may subject our PRC resident shareholders or us to penalties and fines, and limit our ability to inject capital into our PRC subsidiaries, limit our subsidiaries' ability to increase their registered capital, distribute profits to us, or otherwise adversely affect us.

Regulations of Internet Business in China

The PRC government heavily regulates the Internet sector in China, including the legality of foreign investments in the PRC Internet sector, the permit requirements for companies in the Internet industry and the existence and enforcement of restrictions on Internet content and licensing. See Item 4. Information on the Company B. Business Overview Government Regulations.

In order to comply with restrictions imposed by current PRC laws and regulations on foreign ownership of Internet content provision, Internet culture operation, Internet publishing and advertising businesses in China, we operate our PRC online gaming and Internet content provision businesses through contractual arrangements with Shanghai IT and Shanghai Jiucheng Advertisement. Shanghai IT and Shanghai Jiucheng Advertisement are ultimately owned by Jun Zhu and Yong Wang, our shareholders, both of whom are PRC citizens.

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In April 2001, the PRC government began tightening its supervision of Internet cafés, closing unlicensed Internet cafés, requiring those remaining open to install software to prevent access to sites deemed subversive and requiring web portals to sign a pledge not to host subversive sites. Furthermore, the PRC government's policy, which encourages the development of a limited number of national and regional Internet café chains and discourages the establishment of independent Internet cafés, may slow down the growth of Internet cafés. The issuance of Internet café licenses has been suspended from time to time and was suspended most recently in 2007. As Internet cafés are the primary venue for users to play our games, any reduction in the number, or any slowdown in the growth of Internet cafés in China, or any tightening of the governmental requirements relating to the customer's age, business hours and other operational aspects of Internet cafés, could limit our ability to maintain or increase our revenues and expand our customer base, which will materially and adversely affect our business and results of operations. Furthermore, the Ministry of Culture has issued a notice to require, among other things, the review and prior approval of all new online games licensed from foreign game developers and related license agreements. The pre-approval will not be granted if the Ministry of Culture finds the content of the game objectionable or the terms of the related license agreement grossly unfairly to the Chinese licensee. There is no assurance that we will be able to obtain the pre-approvals for our new licensed foreign games in a timely manner.

In 2007, various governmental authorities, including the General Administration of Press and Publication, the Ministry of Industry and Information Technology, the Ministry of Education, the Ministry of Public Security, and other relevant authorities jointly issued a circular concerning the mandatory implementation of an anti-fatigue system in online games, which aimed to protect the physical and psychological health of minors. This law required all online games to incorporate an anti-fatigue system and an identity verification system, both of which have limited the amount of time that a minor or other users may continuously spend playing an online game. We have implemented such anti-fatigue and identification systems on all of our online games. Further strengthening of such anti-fatigue and identification systems or the implementation of any other measures required by any new regulations the PRC government may enact to further tighten its administration of the Internet and online games, and its supervision of Internet cafés, may limit or slow down our prospects for growth, or may materially and adversely affect our business results. See Item 3. Key Information D. Risks Factors Risks Related to Doing Business in China Our business may be adversely affected by public opinion and government policies in China.

Certain PRC regulatory authorities have published regulations that subject website operators to potential liability for content included on their websites and the actions of users and others using their systems. As these regulations are relatively new and subject to interpretation by the relevant authorities, it may not be possible for us to determine in all cases the type of content that could result in liability for us as a website operator. To the extent PRC regulatory authorities find any portion of our content objectionable, they may require us to limit or eliminate the dissemination of such information or otherwise curtail the nature of such content on our websites, which may reduce our user traffic. In addition, we may be subject to significant penalties for violations of those regulations arising from information displayed on, retrieved from or linked to our websites, including a suspension or shutdown of our operations.

Income and Sales Taxes

The National People's Congress of the PRC adopted and promulgated the New Corporate Income Tax Law, or CIT Law, on March 16, 2007. The CIT Law went into effect as of January 1, 2008, and unified the tax rate generally applicable to both domestic and foreign-invested enterprises in the PRC. Our company's subsidiaries and affiliated entities in the PRC are generally subject to CIT at a statutory rate of 25%. However, some subsidiaries that are located in the Pudong New District of Shanghai, and which were established after March 2007, can enjoy five-year transitional reduced EIT rates, which refer to the phase-in rates of 18%, 20%, 22%, 24% and 25% for the five years from 2008 to 2012 according to local practice. Our subsidiaries that hold a HNTE qualification are subject to a 15% preferential EIT rate.

Pursuant to the new PRC CIT Law, companies established in China are generally subject to the CIT at a statutory rate of 25%, while The9 Computer and C9I Shanghai were subject to an 20% EIT rate for the year ended December 31, 2009 due to the local practice of the Pudong New District of Shanghai, where they are located. Shanghai Jincheng Advertisement, which was established after March 2007, was subject to a 25% EIT for the year ended December 31, 2008.

In April 2008, certain government authorities announced the new implementation rules for application and assessment of HNTE. Every qualified HNTE company needs to re-apply for this qualification according to the new implementation rules. C9I Beijing re-applied for the HNTE qualification, received approval from certain government authorities, and can continue to enjoy the EIT exemption for 2008 and 2009 and a 50% reduction of the statutory rate in the three years thereafter. Also, Shanghai IT received approval from certain government authorities to be classified as a HNTE. This approval, subject to annual inspection, entitles Shanghai IT to enjoy a 15% preferential EIT rate for a period of three years.

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The HNTE qualification will be valid for three years after the issuance of the certificate. The enterprise shall apply for re-examination before the term expires. We cannot assure you that our PRC subsidiaries or affiliated entities will meet the criteria to be qualified as HNTEs.

In addition, under the CIT Law, enterprises organized under the laws of their respective jurisdictions outside the PRC may be classified as either non-resident enterprises or resident enterprises. Non-resident enterprises are subject to withholding tax at the rate of 20% with respect to their PRC-sourced dividend income if they have no establishment or place of business in the PRC or if such income is not related to their establishment or place of business in the PRC, unless otherwise exempted or reduced according to treaties or arrangements between the PRC central government and the governments of other countries or regions. The State Council has reduced the withholding tax rate to 10% in the newly promulgated implementation rules of the CIT Law. As we are incorporated in the Cayman Islands, we may be regarded as a non-resident enterprise. We hold The9 Computer and C9I through GameNow.net (Hong Kong) Ltd., and China The9 Interactive Limited. GameNow.net (Hong Kong) Ltd. and China The9 Interactive Limited are companies incorporated in Hong Kong. According to the Tax Agreement between the PRC and Hong Kong, dividends paid by a foreign-invested enterprise in the PRC to its corporate shareholder in Hong Kong holding 25% or more of its equity interest may be subject to withholding tax at the maximum rate of 5% if certain criteria are met. Entitlement to such lower tax rate on dividends according to tax treaties or arrangements between the PRC central government and governments of other countries or regions is further subject to approval of relevant tax authority.

Furthermore, the State Administration of Taxation promulgated the Notice on How to Understand and Determine the Beneficial Owners in Tax Agreement in October 2009, or Circular 601, which provides guidance for determining whether a resident of a contracting state is the beneficial owner of an item of income under China's tax treaties and tax arrangements. According to Circular 601, a beneficial owner generally must be engaged in substantive business activities. An agent or conduit company will not be regarded as a beneficial owner and, therefore, will not qualify for treaty benefits. The conduit company normally refers to a company that is set up for the purpose of avoiding or reducing taxes or transferring or accumulating profits. We cannot assure you that any dividends to be distributed by us to our non-PRC shareholders and ADS holders whose jurisdiction of incorporation has a tax treaty with China providing a different withholding arrangement will be entitled to the benefits under the relevant withholding arrangement.

However, the new law deems an enterprise established offshore but having its management organ in the PRC as a resident enterprise that will be subject to PRC tax at the rate of 25% on its global income. Under the Implementation Rules of the New Enterprise Income Tax Law, the term management organ is defined as an organ which has substantial and overall management and control over the manufacturing and business operation, personnel, accounting, properties and other factors. On April 22, 2009, the State Administration of Taxation further issued a notice regarding recognizing an offshore-established enterprise controlled by PRC shareholders as a resident enterprise according to its management organ. According to this notice, a foreign enterprise controlled by a PRC company or a PRC company group shall be deemed a PRC resident enterprise, if (i) the senior management and the core management departments in charge of its daily operations are mainly located and function in the PRC; (ii) its financial decisions and human resource decisions are subject to the determination or approval of persons or institutions located in the PRC; (iii) its major assets, accounting books, company seals, minutes and files of board meetings and shareholders meetings are located or kept in the PRC; and (iv) more than half of the directors or senior management with voting rights reside in the PRC. Although our offshore companies are not controlled by any PRC company or PRC company group, we cannot assure you that we will not be deemed to be a resident enterprise under the CIT Law and thus be subject to PRC enterprise income tax on our global income.

According to the CIT Law and its implementation rules, dividends are exempted from income tax if such dividends are received by a resident enterprise on equity interests it directly owns in another resident enterprise. However, if we are deemed to be resident enterprise, foreign corporate holders of our shares or ADSs may be subject to taxation at a rate of 10% on any dividends received from us or any gains realized from the transfer of our shares or ADSs.

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The continued eligibility of such preferential tax treatments Shanghai IT, The9 Computer, C9I Shanghai and C9I Beijing enjoyed before 2008 are subject to the implementation of the CIT Law and other relevant regulations, and most of our PRC subsidiaries may no longer be entitled to such tax benefits. Under the CIT Law and related detailed implementation guidance enacted so far, C9I Beijing is entitled to continue its tax holiday of six years (including three years of exemption from CIT followed by three years of a 50% reduction in the CIT rate since 2007); Shanghai IT is entitled to enjoy a preferential EIT rate from 2008 to 2010; and C9I Beijing is entitled to enjoy a preferential EIT rate of 15% for a three year period if it can continuously be qualified as a HNTE. See Item 3. Key Information D. Risk Factors Risks Related to Our Company New income tax laws may increase our tax burden or the tax burden on the holders of our shares or ADSs, and tax benefits available to us may be reduced or repealed, causing the value of your investment in us to suffer.

Critical Accounting Policies

We prepare financial statements in conformity with U.S. Generally Accepted Accounting Principles, which requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities on the date of the financial statements, and the reported amounts of revenue and expenses during the financial reporting period. We continually evaluate these estimates and assumptions based on the most recently available information, our own historical experience and various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates. Some of our accounting policies require higher degrees of judgment than others in their application. We consider the policies discussed below to be critical to an understanding of our financial statements as their application assists management in making their business decisions.

Revenue Recognition. We generate revenue primarily from the sale of our prepaid game cards and prepaid online points for our online game services products to distributors who in turn ultimately sell them to customers. There are two consumption models for our online game services.

Time consumption model – WoW services

We recognize revenue based on the amount of time our customers spend playing our games. Both prepaid cards and prepaid online points provide customers with a certain amount of game playing time that may be used for a pre-specified period of time. All prepaid fees received from distributors are initially recognized as advances from customers recorded on our balance sheet. Prepaid fees are recognized as deferred revenue upon the customers' online registration and activation of their cards or online points. Deferred revenue is recognized as revenue upon the actual usage of the game playing time by customers, when customers are no longer entitled to access our online games, or when the likelihood that we would provide further online game service to those customers becomes remote.

First-time game players are required to purchase CD-Key in order to register a unique code for future game playing. We determine whether an arrangement with multiple deliverables consists of more than one unit of accounting and whether such arrangement should be allocated among the separate units of accounting. Determining whether an arrangement consists of more than one unit of accounting and how consideration should be allocated among the separate units of accounting require significant judgment, including judgment with regard to whether the delivered item(s) has value to the customer on a stand-alone basis and the fair value of the undelivered item. Different judgments may result in different amounts and timing of revenue recognized. Such CD-Key fees received from distributors are initially recognized as advances from customers. Prior to 2008, CD-Key fees were amortized over a one-year period. Effective January 1, 2008, we amortized CD-Key fees over the shorter of one year or WoW's remaining license period, starting from the time when the game players activate the CD-Key. CD-Key fees are also recognized as revenues when the likelihood that they will provide further online game service to customers is remote.

Virtual item / service consumption model – other online game services

We also charge our customers for purchases of services and virtual items. In some of our games, players can access the games free of charge but are charged certain game points for in-game premium features. Prepaid fees are deferred when received and revenue is recognized over the life of the premium features or as the premium features are used. We started charging our customers for purchases of services and virtual items in 2006, and did not recognize

significant revenue from such sales in the year ended December 31, 2006. In 2007, 2008 and 2009, RMB88.2 million, RMB141.2 million and RMB80.8 million (US\$11.8 million), respectively, in net revenue was recognized under this model.

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Product Development. We recognize software development costs for development of software, including online games, to be sold or marketed to customers. As such, we expense software development costs incurred prior to technological feasibility. Once a software product has reached technological feasibility, all subsequent software costs for that product are capitalized until that product is released for sale or available for marketing. After an online game is released, the capitalized product development costs are amortized over the estimated product life. The determination of whether an online game has reached technical feasibility requires significant judgment by us. To date, we have essentially completed our software development concurrently with the establishment of technological feasibility, and, accordingly, no such costs have been capitalized.

For website and internally used software development costs, we expense all costs that are incurred in connection with the planning and implementation phases of development and costs that are associated with repair or maintenance of the existing websites and software. Costs incurred in the development phase are capitalized and amortized over the estimated product life. Since our inception, the amount of costs qualifying as capitalization has been immaterial, and as a result, all website and internally used software development costs have been expensed as incurred.

Income Taxes. We account for income taxes under the asset and liability method. Deferred taxes are determined based upon the differences between the carrying value of assets and liabilities for financial reporting and tax purposes at currently enacted statutory tax rates for the years in which the differences are expected to reverse. The effect on deferred taxes of a change in tax rates is recognized in income in the period of change.

A valuation allowance is provided on deferred tax assets to the extent that it is more likely than not that such deferred tax assets will not be realized. Realization of the future tax benefits related to the deferred tax assets is dependent on many factors, including our ability to generate taxable income within the period during which the temporary differences reverse or our tax loss carry forwards expire, the outlook for the PRC economic environment, and the overall future industry outlook. We consider these factors in reaching our conclusion on the recoverability of the deferred tax assets and determine the valuation allowances necessary at each balance sheet date.

We recognize the impact of an uncertain income tax position at the largest amount that is more-likely-than- not to be sustained upon audit by the relevant tax authority. As of December 31, 2008 and 2009, we did not have any material liability for uncertain tax positions. Our policy is to recognize, if any, tax related interest as interest expenses and penalties as income tax expense. For the years ended December 31, 2007, 2008 and 2009, we did not have any material interest and penalties associated with tax positions.

Property, Equipment and Software. The carrying value of property, equipment and software is impacted by a number of estimates and assumptions, including estimated useful lives, residual values and impairment charges. A review of long-lived assets for impairment is required whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable from its undiscounted future cash flows. In 2007, we did not recognize any impairment charges for property, equipment and software. In 2008 and 2009, we recognized impairment provision on computer equipment of RMB8.9 million and RMB21.2 million (US\$3.1 million), respectively. Recognition of impairment charges requires significant judgment. Any material differences to the estimates that have been used could result in differences in the amount and timing of the impairment charges.

Our computers and equipment for our online game operation are amortized over an estimated useful life of approximately three to four years. Prior to the third quarter of 2007, the servers used for WoW were amortized over WoW's remaining license period of four years commencing from June 2005. In the third quarter of 2007, considering the nature of the assets, server specifications of games to be launched and industry practice, the depreciation lives of all the servers was changed to a consistent period of four years. This was accounted for prospectively from July 1, 2007 as a change in accounting estimate. The depreciation charge relating to this change decreased depreciation expense by approximately RMB25.9 million in year 2007. This was accounted for prospectively from July 1, 2007.

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In connection with the expiration and non-renewal of the WoW license, we assessed alternative uses for equipment used in connection with the operation of WoW, taking into consideration future expected game operations, as well as expected value upon the expiration date of the WoW license agreement. As a result, the expected useful life of the servers and related equipment and the expected value of the servers and related equipment upon termination of the WoW license agreement were adjusted. This change in accounting estimate was accounted for prospectively from January 1, 2008. As a result, depreciation expense relating to this change in year 2008 is to increase depreciation expense recorded as cost of services by approximately RMB68.4 million, to decrease both profit from operations and net income by RMB68.4 million, and to decrease both basic and diluted earnings per share by RMB2.47. Depreciation expense relating to this change in year 2009 is to increase depreciation expense recorded as cost of services by approximately RMB40.0 million (US\$5.9 million), to increase both loss from operations and net loss by RMB40.0 million (US\$5.9 million), and to increase both basic and diluted net loss per share by RMB1.57.

Intangible assets. Our intangible assets consist primarily of intangible assets from business combination and upfront licensing fees. We recognize intangible assets acquired through business acquisitions as assets separate from goodwill if they satisfy either the contractual-legal or separability criterion. Intangible assets with definite lives are amortized over their estimated useful lives and reviewed for impairment in accordance with relevant accounting guidance. Intangible assets, such as purchased technology, licenses, domain names and non-compete agreements, arising from the acquisitions of subsidiaries and variable interest entities are recognized and measured at fair value upon acquisition. The WoW game related intangible assets arising from such business combination transaction were amortized over the licensing term of the WoW game of four years.

Upfront licensing fees paid to licensors are recognized as intangible assets if a game has reached technological feasibility when such payments are contractually due. Technological feasibility is met upon completion of a working model. Upfront licensing fees are amortized on a straight-line basis over the shorter of the useful economic life of the relevant online game or license period, which range from two to four years. Amortization of the upfront licensing fees commences upon the launch of the applicable online game.

Goodwill. Goodwill represents the excess of the purchase price over the fair value of the identifiable assets and liabilities acquired as a result of an acquisition we make. Goodwill is not amortized, but tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired. In December of each year, we test impairment of goodwill at the reporting unit level and recognize impairment in the event that the carrying value exceeds the fair value of each reporting unit. Goodwill impairment assessment requires significant judgment, including assumptions used to determine the fair value of the reporting units. We determine the fair value of our reporting units based on the present value of estimated future cash flows of the reporting units. If the carrying amount is in excess of the fair value, step two requires the comparison of the implied fair value of the reporting unit's goodwill with the carrying amount of the reporting unit's goodwill. Any excess of the carrying value of the reporting unit's goodwill over the implied fair value of the reporting unit's goodwill is recorded as an impairment loss. After completing our annual impairment reviews during the fourth quarters of 2007 and 2008, we concluded that goodwill was not impaired in fiscal 2007 and 2008. In June 2009, we assessed the recoverability of goodwill and recognized full impairment of RMB30.2 million (US\$4.4 million), as a result of the non-renewal of WoW license.

Share-Based Compensation. We granted a total of 1,197,500 options in 2007, 205,000 options in 2008 and no new option in 2009 under our Amended 2004 Stock Option Plan to certain of our employees and directors. On September 1, 2009, we modified the exercise price of stock options granted to certain senior officers and directors to US\$7.36 per share, the market price on the date of modification.

We measure the cost of employee services received in exchange for stock-based compensation measured at the grant date fair value of the award. For the awards that are modified, we determine the incremental cost as the excess of the fair value of the modified award over the fair value of the original award immediately before its terms are modified, measured based on the share price and other pertinent factors at that date. We recognize the compensation costs, net of the estimated forfeiture, on a straight-line basis over the vesting period of the award, which generally ranges from two to four years. Forfeiture rates are estimated based on historical forfeiture patterns and adjusted to reflect future changes in circumstances and facts, if any. If actual forfeitures differ from those estimates, the estimates may be revised in subsequent periods. We use historical data to estimate pre-vesting option forfeitures and record stock-based

compensation expense only for those awards that are expected to vest.

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Determining the fair value of stock options requires significant judgment. We measure the fair value of the stock options using the Black-Scholes option-pricing model with assumptions made regarding expected term, volatility, risk-free interest rate, and dividend yield. The expected term represents the period of time that the awards granted are expected to be outstanding. The expected term is determined based on historical data on employee exercise and post-vesting employment termination behavior, or the simplified method for stock option awards with the characteristics of plain vanilla options for 2007, 2008 and 2009. Expected volatilities are based on historical volatilities of our ordinary shares and with consideration of historical volatilities of comparable companies. Risk-free interest rate is based on US government bonds issued with maturity terms similar to the expected term of the stock-based awards. While we paid a discretionary cash dividend in January 2009, we do not anticipate paying any recurring cash dividends in the foreseeable future.

Other than the options granted under our Amended 2004 Stock Option Plan, in November 2008, as approved by our board of directors, we granted equity warrants to IncSight Limited, or IncSight, a company wholly-owned by Jun Zhu, our chairman and chief executive officer, to purchase 552,196 of our ordinary shares. Also, in September 2008, TDC, a wholly-owned subsidiary of our company, approved its 2008 Stock Option Plan, or the TDC Option Plan. On October 1, 2008, TDC granted options to Jun Zhu and certain employees of TDC to purchase 18,961 ordinary shares of TDC. We recorded share-based compensation for these equity warrants and TDC options in 2008 and 2009. Share-based compensation expenses of RMB46.7 million, RMB52.0 million and RMB71.2 million (US\$10.4 million) were recognized for the years ended December 31, 2007, 2008 and 2009, for options and warrants granted to our company's employees and directors, including incremental compensation cost of RMB13.4 million (US\$2.0 million) in 2009 due to modification of the option exercise price.

Available-for-sale investments. Investments in debt and equity securities are, on initial recognition, classified into the three categories: held-to-maturity securities, trading securities and available-for-sale securities. Debt securities that our company has the positive intent and ability to hold to maturity are classified as held-to-maturity securities and reported at amortized cost. Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings. Debt and equity securities not classified as either held-to-maturity securities or trading securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses recognized in equity. We classify our investments in preferred shares and convertible loan of Infocomm Asia Holdings Pte Ltd. and preferred shares of Ideas Corporation as available-for-sale securities and hence these investments were stated at fair value on our balance sheets. As of December 31, 2008 and 2009, we did not hold trading securities or held-to-maturity securities.

When we determine that the impairment of an available-for-sale equity security is other-than-temporary, we recognize an impairment loss in earnings equal to the difference between the investment's cost and its fair value at the balance sheet date of the reporting period for which the assessment is made. When other-than-temporary impairment has occurred for an available-for-sale debt security, and we intend to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, we recognize an impairment loss in earnings equal to the difference between the investment's amortized cost basis and its fair value at the balance sheet date. To determine whether a loss is other-than-temporary, we review the cause and duration of the impairment, the extent to which fair value is less than cost, the financial condition and near-term prospects of the issuer, and our intent and ability to hold the security for a period of time sufficient to allow for any anticipated recovery of its amortized cost. As a result of our assessment of the recoverability of our investments, we recognized impairment of RMB14.6 million and RMB36.0 million (US\$5.3 million) in 2008 and 2009, respectively. Of the RMB36.0 million impairment in 2009, RMB22.4 million (US\$3.3 million) impairment loss was recorded in earnings and RMB13.6 million (US\$2.0 million) was unrealized gain reversed from accumulated other comprehensive income.

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Impairment of Equity Investment. We assess our equity investments for other-than-temporary impairment by considering factors as well as all relevant and available information including, but not limited to, current economic and market conditions, the operating performance of the investee, including current earnings trends, and other company-specific information including recent financing rounds. Impairment provision relating to investment in an equity investee of RMB0.6 million, RMB11.3 million and nil was recognized in 2007, 2008 and 2009, respectively.

Impairment of Long-lived Assets and Intangible Assets. We review long-lived assets and intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. We assess the recoverability of long-lived assets and intangible assets (other than goodwill) by comparing the carrying amount to the estimated future undiscounted cash flow associated with the related assets. We recognize impairment of long-lived assets and intangible assets in the event that the net book value of such assets exceeds the estimated future undiscounted cash flow attributable to such assets. We use estimates and judgment in our impairment tests, and if different estimates or judgments had been utilized, the timing or the amount of the impairment charges could be different. Impairment charges relating to long-lived assets amounting to nil, RMB8.9 million and RMB21.1 million (US\$3.1 million) were recognized in 2007, 2008 and 2009, respectively. Impairment charges relating to intangible assets amounting to RMB18.7 million, RMB73.2 million and RMB27.5 million (US\$4.0 million) were recognized in 2007, 2008 and 2009, respectively.

Noncontrolling interest. On January 1, 2009, we adopted FASB Accounting Standards Codification, ASC 810-10-65, Consolidations – Overall Transition and Open Effective Date Information (previously Statement of Financial Accounting Standards or SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51). A noncontrolling interest in our subsidiary or variable interest entity represents the portion of the equity (net assets) in the subsidiary or variable interest entity not directly or indirectly attributable to us. This pronouncement requires noncontrolling interests to be presented as a separate component of equity in the consolidated balance sheet and modifies the presentation of net income by requiring earnings and other comprehensive income to be attributed to controlling and noncontrolling interest. The presentation regarding noncontrolling interest was retrospectively applied for all the periods presented.

Results of Operations

The following table sets forth a summary of our consolidated statements of operations as a percentage of net revenues for the periods indicated.

	Year Ended December 31,	
	2007	2008