

GIGAMEDIA Ltd  
Form 20-F  
April 30, 2013  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, D. C. 20549

**FORM 20-F**

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

For the fiscal year ended December 31, 2012

Commission File Number: 000-30540

**GIGAMEDIA LIMITED**

(Exact name of registrant as specified in its charter)

**REPUBLIC OF SINGAPORE**

(Jurisdiction of incorporation or organization)

**8<sup>TH</sup> FLOOR, NO. 22, LANE 407, SECTION 2 TIDING BOULEVARD, TAIPEI, TAIWAN, R.O.C.**

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(Address of principal executive offices)

**COLLIN HWANG, Chief Executive Officer**

**8<sup>TH</sup> FLOOR, NO. 22, LANE 407, SECTION 2 TIDING BOULEVARD, TAIPEI, TAIWAN, R.O.C.**

**Tel: 886-2-2656-8000; Fax: 886-2-2656-8003**

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

| <b>Title of Each Class</b> | <b>Name of Each Exchange on Which Registered</b> |
|----------------------------|--|
| <b>Ordinary Shares</b>     | <b>The NASDAQ Stock Market LLC</b>               |

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

**None**

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

**None**

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

**50,719,976 ordinary shares**

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

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

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

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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

Other

by the International Accounting Standards Board

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

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

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**Table of Contents****CERTAIN TERMS AND CONVENTIONS**

In this annual report, all references to (i) we, us, our, our Company or GigaMedia are to GigaMedia Limited and, unless the context requires otherwise, its subsidiaries, or where the context refers to any time prior to the incorporation of any of its subsidiaries, the businesses which predecessors of the present subsidiaries were engaged in and which were subsequently assumed by such subsidiaries; (ii) Shares are to ordinary shares of our Company; (iii) Hoshin GigaMedia are to Hoshin GigaMedia Center Inc., a company incorporated under the laws of Taiwan, Republic of China, ( Taiwan or R.O.C. ); (iv) FunTown are to our Asian online game and service business operated through our two operating subsidiaries, Hoshin GigaMedia and FunTown World Limited, a company incorporated under the laws of the British Virgin Islands; (v) GigaMedia Cloud are to GigaMedia Cloud Services Co. Ltd., a company incorporated under the laws of Taiwan; (vi) GigaCloud are to the cloud computing services operated through our subsidiary GigaMedia Cloud; (vii) IAH or IAHHGames are to Infocomm Asia Holdings Pte. Ltd., an online game operator, publisher and distributor in Southeast Asia and incorporated under the laws of the Republic of Singapore; (viii) Monsoon are to Monsoon Online Pte. Ltd., a company incorporated under the laws of the Republic of Singapore and wholly owned by IAHHGames; (ix) T2CN are to T2CN Holding Limited, a company incorporated under the laws of the British Virgin Islands, and the T2CN Operating Entities; (x) T2CN Operating Entities are to T2CN Holding Limited's two wholly owned subsidiaries, T2CN Information Technology (Shanghai) Co., Ltd. ( T2 Technology ) and J-Town Information (Shanghai) Co., Ltd. ( J-Town ), and three variable interest entities, Shanghai T2 Entertainment Co., Ltd. ( T2 Entertainment ), Shanghai T2 Advertisement Co., Ltd. ( T2 Advertisement ) and Shanghai Jinyou Network & Technology Co., Ltd. ( Jinyou ); (xi) Internet access and service business are to an Internet access and service business that we historically operated through Koos Broadband Telecom Co., Ltd. ( KBT ) and completely disposed of in September 2008; (xii) UIM are to Ultra Internet Media S.A., a company incorporated under the laws of Nevis; (xiii) Everest Gaming are to Mangas Everest S.A.S, a société par actions simplifiée registered with the Trade and Companies Registry of Paris and organized under the laws of France; (xiv) BetClic are to BetClic Everest Group, formerly named as Mangas Gaming S.A.S, a company organized under the laws of France; (xv) JIDI are to JIDI Network Technology (Shanghai) Co., Ltd., our wholly owned subsidiary incorporated under the laws of the PRC; and (xvi) Shanghai JIDI are to Shanghai JIDI Network Technology Co., Ltd., a company incorporated under the laws of the PRC.

For the purpose of this annual report only, geographical references to China and the PRC are to the People's Republic of China and do not include Taiwan, the Hong Kong Special Administrative Region ( Hong Kong ) and the Macau Special Administrative Region ( Macau ). Except if the context otherwise requires, and for the purpose of this annual report only, references to Greater China include the PRC, Taiwan, Hong Kong and Macau. References to South Korea are to the Republic of Korea.

All references in this annual report to U.S. dollar, \$ and US\$ are to the legal currency of the United States; all references to NT dollar or New Taiwan dollar are to the legal currency of Taiwan; all references to RMB, Rmb or Renminbi are to the legal currency of the PRC; all references to Hong Kong dollar are to the legal currency of Hong Kong and all references to Singapore dollar and S\$ are to the legal currency of the Republic of Singapore.

We have approximated certain numbers in this annual report to their closest round numbers or a given number of decimal places. Due to rounding, figures shown as totals in tables may not be arithmetic aggregations of the figures preceding them.

**DISCLOSURE REGARDING FORWARD-LOOKING STATEMENTS**

This annual report includes forward-looking statements within the meaning of, and intended to qualify for the safe harbor from liability established by, the United States Private Securities Litigation Reform Act of 1995. These statements, which are not statements of historical fact, may consist of or contain estimates, assumptions, projections and/or expectations regarding future events, which may or may not occur. These statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Some of the risks are listed under Item 3, Key Information D. Risk Factors and elsewhere in this annual report. In some cases, you can identify these forward-looking statements by words such as anticipate, believe, could, estimate, expect, intend, may, plan, potential, should, similar expressions, including their negatives. These forward-looking statements include, without limitation, statements relating to:

our business plan and strategies;

our future business development and potential financial condition, results of operations and other projected financial information;

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our ability to manage current and potential future growth;

expected continued acceptance of our revenue model;

our plans for strategic partnerships, licenses and alliances;

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our acquisition and strategic investment strategy, and our ability to successfully integrate any past, current, or future acquisitions into our operations;

our ability to protect our intellectual property rights and the security of our customers' information;

the launch of new online games according to our timetable;

expected continued acceptance of our online games, including expected growth of the online games industry, and consumer preferences for our products and services;

the in-house development of new online games;

our plans to license additional games from third parties, and the launch of these new games, including the timing of any such development, licenses or launches, in various geographic markets;

our ability to maintain and strengthen our position as one of the largest online MahJong operators in Taiwan;

the potential entry of new competitors in any of our business lines;

changes in the global regulatory environment relating to the online gaming business;

changes or stability in certain regulatory environments relating to GigaCloud's operations;

changes in PRC laws and regulations, and future enforcement of those laws and regulations, including laws and regulations relating to Internet usage, advertising over the Internet, Internet content providers, foreign investment and ownership in online business, distribution of dividends and foreign exchange controls;

the outcome of ongoing, or any future, litigation or arbitration; and

our corporate classification by various governmental entities.

These forward-looking statements are based on our own information and on information from other sources we believe to be reliable. Our actual results may differ materially from those expressed or implied by these forward-looking statements as a result of risk factors and other factors noted throughout this annual report, including those described under Item 3, "Key Information" D. Risk Factors and those detailed from time to time in other filings with the United States Securities and Exchange Commission (the "SEC"). We do not guarantee that the transactions and events described in this annual report will happen as described or that they will happen at all. We undertake no obligation to update or revise any forward-looking statements to reflect events or circumstances after the date of this annual report or to reflect the occurrence of unanticipated events. Whether actual results will conform to our expectations and predictions is subject to a number of risks and uncertainties, many of which are beyond our control, and reflect future business decisions that are subject to change. Given this level of uncertainty, you are advised not to place undue reliance on such forward-looking statements.





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**PART I**

**ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not applicable, but see Item 6, Directors, Senior Management and Employees A. Directors and Senior Management in this annual report.

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not applicable.

**ITEM 3. KEY INFORMATION**

**Exchange Rates**

Assets and liabilities on our balance sheet denominated in currencies other than U.S. dollars are translated into U.S. dollars using year-end exchange rates. Income and expense items in our statement of income (loss) denominated in currencies other than U.S. dollars are translated into U.S. dollars using weighted-average exchange rates. Certain other operating financial information denominated in currencies other than U.S. dollars, not included in our consolidated financial statements and provided in this annual report, are translated using weighted-average exchange rates. For convenience, transactions in 2013 denominated in currencies other than U.S. dollars have been translated into U.S. dollars using the year-end exchange rate for 2012 published by the Bank of Taiwan. We make no representation that any currencies other than U.S. dollars could be converted to U.S. dollars at such rate or any particular rates.

**A. Selected Financial Data**

The following selected consolidated balance sheet data as of December 31, 2011 and 2012 and the selected consolidated statement of income (loss) data for the years ended December 31, 2010, 2011 and 2012 have been derived from our audited consolidated financial statements included in Item 18 in this annual report. The selected consolidated balance sheet data as of December 31, 2008, 2009 and 2010, and the selected consolidated statement of income (loss) data for the years ended December 31, 2008 and 2009 have been derived from our audited consolidated financial statements for the years ended December 31, 2008, 2009 and 2010, which are not included in this annual report. The consolidated financial statements have been prepared and presented in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. You should read the following selected consolidated financial data in conjunction with Item 5, Operating and Financial Review and Prospects, and the consolidated financial statements and the accompanying notes to those statements included in this annual report. The statement of income (loss) for the year ended December 31, 2011 has been restated to reflect the results of JIDI, which our board of directors resolved in June 2012 to liquidate and disposed of, as discontinued operations. Certain prior-year amounts have been reclassified to conform to the current-year presentation. These reclassifications had no effect on the results of operations or shareholders' equity as previously reported.

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(in thousands except for earnings per share amounts)

|  | 2008<br>US\$     | 2009<br>US\$     | 2010<br>US\$    | 2011<br>US\$    | 2012<br>US\$    |
|--|------------------|------------------|-----------------|-----------------|-----------------|
| <b>STATEMENT OF INCOME (LOSS) DATA:</b>  |                  |                  |                 |                 |                 |
| <b>OPERATING REVENUES</b>  |                  |                  |                 |                 |                 |
| Gaming software and service revenues   | 144,765          | 112,694          | 25,820          | 0               | 0               |
| Asian online game and service revenues   | 45,604           | 46,887           | 38,862          | 34,367          | 27,470          |
| <b>Total operating revenues</b>  | <b>190,369</b>   | <b>159,581</b>   | <b>64,682</b>   | <b>34,367</b>   | <b>27,470</b>   |
| <b>OPERATING COSTS</b>   |                  |                  |                 |                 |                 |
| Cost of gaming software and service revenues   | (22,770)         | (20,102)         | (4,010)         | 0               | 0               |
| Cost of Asian online game and service revenues   | (12,404)         | (16,785)         | (17,103)        | (14,413)        | (11,388)        |
| <b>Total operating costs</b>   | <b>(35,174)</b>  | <b>(36,887)</b>  | <b>(21,113)</b> | <b>(14,413)</b> | <b>(11,388)</b> |
| <b>GROSS PROFIT</b>  | <b>155,195</b>   | <b>122,694</b>   | <b>43,569</b>   | <b>19,954</b>   | <b>16,082</b>   |
| <b>OPERATING EXPENSES</b>  |                  |                  |                 |                 |                 |
| Product development and engineering expenses   | (13,455)         | (14,195)         | (7,301)         | (1,956)         | (1,471)         |
| Selling and marketing expenses   | (74,173)         | (79,421)         | (21,589)        | (10,079)        | (8,377)         |
| General and administrative expenses  | (25,035)         | (29,692)         | (31,780)        | (18,101)        | (13,384)        |
| Bad debt expenses  | (2,905)          | (1,092)          | (1,639)         | (1,820)         | (169)           |
| Impairment loss on property, plant, and equipment  | 0                | (1,250)          | (278)           | 0               | 0               |
| Impairment loss on goodwill  | 0                | (14,103)         | (2,255)         | (5,097)         | (12,489)        |
| Impairment loss on intangible assets   | (641)            | (4,701)          | (1,330)         | (2,583)         | (15)            |
| Impairment loss on prepaid licensing and royalty fees  | (883)            | (18,301)         | (870)           | (247)           | (702)           |
| Impairment loss on deconsolidation of T2CN   | 0                | 0                | (22,234)        | 0               | 0               |
| Other  | 0                | 0                | (1,989)         | 0               | (49)            |
| <b>Total operating expenses</b>  | <b>(117,092)</b> | <b>(162,755)</b> | <b>(91,265)</b> | <b>(39,883)</b> | <b>(36,656)</b> |
| <b>Income (loss) from operations</b>   | <b>38,103</b>    | <b>(40,061)</b>  | <b>(47,696)</b> | <b>(19,929)</b> | <b>(20,574)</b> |
| <b>Income (loss) from continuing operations</b>  | <b>35,710</b>    | <b>(56,102)</b>  | <b>1,408</b>    | <b>(67,390)</b> | <b>(13,596)</b> |
| <b>Income (loss) from discontinued operations</b>  | <b>9,435</b>     | <b>222</b>       | <b>(128)</b>    | <b>(4,188)</b>  | <b>(2,521)</b>  |
| <b>Net income (loss)</b>   | <b>45,145</b>    | <b>(55,880)</b>  | <b>1,280</b>    | <b>(71,578)</b> | <b>(16,117)</b> |
| <b>Less: Net (income) loss attributable to the noncontrolling interest and subsidiary preferred shares</b> | <b>(757)</b>     | <b>6,795</b>     | <b>1,370</b>    | <b>366</b>      | <b>827</b>      |
| <b>Net income (loss) attributable to GigaMedia</b>   | <b>44,388</b>    | <b>(49,085)</b>  | <b>2,650</b>    | <b>(71,212)</b> | <b>(15,290)</b> |

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|  |      |        |      |        |        |
|--|------|--------|------|--------|--------|
| Earnings (loss) per share (in dollars):    |      |        |      |        |        |
| Basic:                                     |      |        |      |        |        |
| Income (loss) from continuing operations   | 0.65 | (0.90) | 0.05 | (1.23) | (0.25) |
| Income (loss) from discontinued operations | 0.17 | 0.00   | 0.00 | (0.08) | (0.05) |
| Net income (loss)                          | 0.82 | (0.90) | 0.05 | (1.31) | (0.30) |
| Diluted:                                   |      |        |      |        |        |
| Income (loss) from continuing operations   | 0.58 | (0.90) | 0.04 | (1.23) | (0.25) |
| Income (loss) from discontinued operations | 0.16 | 0.00   | 0.00 | (0.08) | (0.05) |
| Net income (loss)                          | 0.74 | (0.90) | 0.04 | (1.31) | (0.30) |

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As of December 31,

(US dollars in thousands except for number of issued shares)

|   | 2008<br>US\$ | 2009<br>US\$ | 2010<br>US\$ | 2011<br>US\$ | 2012<br>US\$ |
|---|--------------|--------------|--------------|--------------|--------------|
| <b>BALANCE SHEET DATA:</b>                                  |              |              |              |              |              |
| Total current assets  | 128,799      | 104,839      | 93,088       | 118,920      | 85,135       |
| Property, plant and equipment-net                           | 13,468       | 5,989        | 5,301        | 4,288        | 1,949        |
| Goodwill  | 87,098       | 44,417       | 39,493       | 28,437       | 16,934       |
| Intangible assets-net                                       | 28,930       | 18,924       | 19,769       | 15,534       | 15,675       |
| Total assets  | 316,793      | 260,181      | 267,589      | 191,706      | 140,394      |
| Net assets  | 237,076      | 186,360      | 216,566      | 154,862      | 117,893      |
| Total GigaMedia s shareholders equity                       | 228,456      | 184,745      | 217,521      | 156,072      | 117,893      |
| Common shares, no par value, and additional paid-in capital | 300,021      | 304,379      | 309,332      | 304,672      | 304,851      |
| Number of issued shares (in thousands)                      | 54,365       | 54,995       | 56,263       | 50,720       | 50,720       |
| Dividends declared per share (in dollars)                   | 0            | 0            | 0            | 0            | 0            |
| Earnings (loss) per share from continuing operations        |              |              |              |              |              |
| Basic   | 0.65         | (0.90)       | 0.05         | (1.31)       | (0.30)       |
| Diluted   | 0.58         | (0.90)       | 0.04         | (1.31)       | (0.30)       |

**B. Capitalization and Indebtedness**

Not applicable.

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

Not applicable.

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### **D. Risk Factors**

#### **Risks Related to Our Business and Industries**

##### **We may not be successful in operating and improving our existing online games to satisfy the changing demands and preferences of players**

The level of demand and market acceptance of our existing online games is subject to a high degree of uncertainty. Our future operating results will depend on numerous factors, many of which are beyond our control. These factors include:

the popularity of existing and new online games operated by us;

the introduction of new online games by us or third parties, competing with or replacing our existing online games;

general economic conditions, particularly economic conditions adversely affecting discretionary consumer spending;

changes in our customer demands and preferences;

regulatory and other risks associated with our operations in Taiwan and Hong Kong;

the availability of other forms of entertainment; and

critical reviews and public tastes and preferences, all of which change rapidly and cannot be predicted.

Our ability to plan for product development and distribution and promotional activities will be significantly affected by how well we anticipate and adapt to relatively rapid changes in consumer tastes and preferences. Currently, a substantial portion of our online games revenue is derived from revenues from our online MahJong games and other casual games offered in Taiwan and Hong Kong by FunTown and from two licensed massively multi-player online (MMO) games, A.V.A. and Tales Runner. However, there is no assurance that these games will continue to be popular. A decline in the popularity of these games, or in the popularity of online games in general, is likely to adversely affect our business, financial condition and results of operations. To maintain competitiveness of our games, we must regularly invest in enhancing, improving, expanding or upgrading our games. If we fail to do so, revenues generated from our existing games will likely decline.

##### **In operating our Asian online game and service business, we may fail to launch new games according to our timetable, and our new games may not be commercially successful**

In order for our Asian online game and service business strategy to succeed over time, we will need to license, acquire or develop new online games that can generate additional revenue and further diversify our revenue sources. A number of factors, including technical difficulties, government approvals and game licenses required for launching new games, lack of sufficient game development personnel and other resources, and adverse developments in our relationship with the licensors of our new licensed games could result in delay in launching our new games. Therefore, we cannot assure you that we will be able to meet our timetable for new game launches.

There are many factors that may adversely affect the popularity of our new games. For example, we may fail to anticipate and adapt to future technical trends and new business models, fail to satisfy game player preferences and requirements, fail to effectively plan and organize marketing and promotion activities, fail to effectively detect and prevent programming errors or defects in the games, and fail to operate our new games at acceptable costs. We cannot assure you that our new games will gain market acceptance and become commercially successful. If we are not able to license, develop or acquire additional online games that are commercially successful, our future revenues and profitability may decline.



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Due to increased competition among online games operators in Greater China, license fees for online games have increased and most licensors are demanding upfront license fees and guaranteed minimum royalty payments. If any of the new games we license from third parties fails to appeal to players, we may not be able to fully recover upfront and/or minimum royalty licensing costs, which can be significant. As a result, our results of operations and financial condition may be materially and adversely affected.

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

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

Our management conducted an evaluation of the effectiveness of our internal control over financial reporting and concluded that as of December 31, 2012, our disclosure controls and procedures were effective in providing reasonable assurance, that information required to be disclosed by us, in the reports that we file or submit under the Exchange Act, was recorded, processed, summarized and reported on a timely basis, and these controls and procedures were effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act was accumulated and communicated to our management as appropriate to allow timely decisions regarding required disclosure.

In the Company's 2010 Annual Report on Form 20-F, the Company reported a material weakness, having found there were inadequate controls in place to address risks related to usurpation of established policies, procedures and control systems related to T2CN. As reported in the Company's 2011 Annual Report on Form 20-F, the Company has undertaken and completed, as appropriate, its testing to validate the effective implementation of certain remedial measures. The Company has also undertaken testing which validates the effective operation of these controls, for a sufficient period of time, to support its conclusion. In reviewing the results from this testing, management has concluded that the material weakness in internal control over financial reporting we previously reported has been remediated as of December 31, 2011.

We have completed our Section 404 assessment under the Sarbanes-Oxley Act and received our auditors' attestation as of December 31, 2012. The report of our independent registered public accounting firm includes an opinion regarding the effectiveness of our internal control over financial reporting. However, internal control over financial reporting may not prevent or detect misstatements because of its inherent limitations, including the possibility of human error, the circumvention or overriding of controls, or fraud. Therefore, even effective internal controls can provide only reasonable assurance with respect to the preparation and fair presentation of financial statements. In addition, projections of any evaluation of effectiveness of internal control over financial reporting to future periods are subject to the risk that the control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

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

### **Our results of operations are subject to significant fluctuations**

Our revenues, expenses and results of operations have varied in the past and may fluctuate significantly in the future due to a variety of factors, many of which are beyond our control. The key factors affecting our businesses include:

Asian online game and service business: our ability to retain existing users; attract new users and maintain user satisfaction; the pace of rolling out new games or updating existing games by us or our competitors; the amount and timing of operating costs and capital expenditures relating to our business operations and expansion; seasonal trends in Internet use; price competition in the industry; regulatory and other risks associated from our operations in Taiwan and Hong Kong.

Cloud computing business: global economic conditions and general economic conditions of the markets that GigaCloud targets; the availability of the Internet infrastructure; and the technological and other competition from existing and new competitors, our ability to attract new users and maintain user satisfaction; the pace of rolling out new products and services or updating existing offerings by us or our competitors; the amount and timing of operating costs and capital expenditures relating to our business operations and expansion; and regulatory risks associated with our operations in Greater China.

In addition, our operating expenses are based on our expectations of the future demand for our services and are relatively fixed in the short term. We may be unable to adjust spending quickly enough to offset any unexpected demand shortfall. A decrease in revenues in relation to our expenses could have a material and adverse effect on our business, results of operations and financial condition. You should not place undue reliance on our financial guidance, nor should you rely on year-to-year or quarter-to-quarter comparisons of our results of operations as indicators of our future performance.

### **Our business strategy, which contemplates growth through acquisitions and strategic investments, exposes us to significant risks**

We have pursued and may continue to pursue growth through acquisitions and strategic investments. Any acquisition or investment is subject to a number of risks. Such risks include the diversion of management time and resources, disruption of our ongoing business, lack of familiarity with new markets, difficulties in supporting the acquired business, and dilution to existing stockholders if our common stock is issued in consideration for an acquisition or investment, incurring or assuming indebtedness or other liabilities in connection with an acquisition.

We entered into multiple strategic alliances in the past and later recorded related impairment losses on investments and goodwill. We may incur debts in the future upon an acquisition or suffer losses related to impairment of these investments. Any impairment on goodwill and marketable securities and investments in the future may have a negative impact on our financial results. We will continue to examine the merits, risks and feasibility of potential transactions, and expect to explore additional acquisition opportunities in the future. Such examination and exploration efforts, and any related discussions with third parties, may or may not lead to future acquisitions and investments. We may not be able to complete acquiring or investing transactions that we initiate. Our ability to grow through such acquisitions and investments will depend on many factors, including the availability of suitable acquisition candidates at an acceptable cost, our ability to reach agreement with acquisition candidates or investee companies on commercially reasonable terms, the availability of financing to complete transactions and our ability to obtain any required governmental approvals.

We also face challenges in integrating any acquired business. These challenges include eliminating redundant operations, facilities and systems, coordinating management and personnel, retaining key employees, managing different corporate cultures, maintaining the relationship with the suppliers, vendors and/or distributors of acquired businesses, and achieving cost reductions and cross-selling opportunities. There can be no assurance that we will be able to successfully integrate all aspects of acquired businesses. The process of integrating the acquired business may disrupt our business and divert our resources. In addition, the benefits of an acquisition or investment transaction may take considerable time to be fully realized and we cannot assure you that any particular acquisition or investment and the subsequent integration will produce the intended benefits.

**The online games market is characterized by rapid technological change, and failure to respond quickly and effectively to new Internet technologies or standards may have a material adverse effect on our business**



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The online games industry is evolving rapidly. Any new technologies and new standards may require increases in expenditures for online game development and operations. In addition, we use internally developed software systems that support nearly all aspects of our billing and payment transactions in our Asian online game and service business. All of our businesses may be adversely affected if we are unable to upgrade our systems effectively to accommodate future traffic levels, to avoid obsolescence or to successfully integrate any newly developed or acquired technology with our existing systems. Capacity constraints could cause unanticipated system disruptions and slower responses, which could adversely affect data transmission and game play. These factors could, among other things, cause us to lose existing or potential users and existing or potential game development partners.

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### **Our business could suffer if we do not successfully manage current growth and potential future growth**

We are pursuing a number of growth strategies. Some of these strategies relate to services, products or markets in which we lack experience and expertise. Anticipated expansion of our operations will place a significant strain on our management, operation systems and resources. In addition to training and managing our workforce, we will need to continue to develop and improve our financial and management controls and our reporting systems and procedures, including those of acquired businesses. We cannot assure you that we will be able to effectively manage the growth of our operations, and any failure to do so may limit our future growth and materially and adversely affect our business, financial condition and results of operations.

### **We recorded net and operating losses in past years, and we may experience losses in the future**

In 2010, 2011 and 2012, we recorded operating losses of US\$47.7 million, US\$24.1 million and US\$7.9 million, as well as net income of \$2.7 million, a net loss of \$71.2 million, and a net loss of \$15.3 million, respectively. Our future profitability will depend to a great extent upon the performance of our Asian online game and service business and the GigaCloud cloud computing business. We cannot assure you that we will not experience operating or net losses in future periods.

### **Our Asian online game and service business faces intense competition, which may adversely affect our revenues, profitability and planned business expansion**

The online games market is highly competitive. Online casual game operators in Greater China are currently our primary competitors. We also compete with massively multi-player online role-playing game ( MMORPG ) operators throughout Greater China. Our major competitors in Taiwan include Gamania Digital Entertainment Co., Ltd. ( Gamania ), Soft-World International Corporation ( Soft-World ), International Games System, Co., Ltd. ( IGS ), UserJoy Technology Co., Ltd. ( UserJoy ) and GodGame Inc. ( GodGame ). Our major competitors in the PRC include Shanda Interactive Entertainment Ltd. ( Shanda ), Giant Interactive Group, Inc. ( Giant ), Changyou.com Limited ( Changyou ), The9 Limited, Shanghai Everstar Online Entertainment Co., Ltd. ( Nineyou ), Tencent Holdings Limited ( Tencent ), Perfect World Co., Ltd. ( Perfect World ), Kingsoft Corporation Limited ( Kingsoft ), Beijing Globalink Computer Technology Co., Ltd.( Ourgames.com ) and Chinagames.net.

In addition, we compete for users against various offline games, such as console games, arcade games and handheld games, as well as various other forms of traditional or online entertainment.

We expect more online games operating companies to enter the markets where we operate in Greater China, and a wider range of online games to be introduced to these markets, given the relatively low entry barriers to the online games industry and the increasing popularity of Internet-based businesses. Our competitors vary in size and include private and public companies, many of which have greater financial, marketing and technical resources as well as name brand recognition. We intend to continue to enhance our market position through providing competitive products and quality services that meet market trends and users' preferences, as well as strengthening sales effectiveness.

As a result of the above, significant competition may 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 have a material adverse effect on our business, financial condition and results of operations.

### **Our Asian online game and service business depends on the reliability of the network infrastructure and related services provided by ourselves and third parties, which is subject to physical, technological, security and other risks**

The development and operation of our online networks are subject to physical, technological, security and other risks which may result in interruption in service or reduced capacity. These risks include physical damage, power loss, telecommunications failure, capacity limitation, hardware or software failures or defects and breaches of physical and cybersecurity by computer viruses, system break-ins or otherwise. An increase in the volume of usage of online services could strain the capacity of the software and hardware employed, which could result in slower response time or system failures. We have a variety of backup servers at our primary site to deal with possible system failures. However, we do not have redundant facilities in the event of an emergency. The occurrence of any of these events could result in interruptions, delays or cessation in service to users of our online services, which could have a material adverse effect on our business and results of operations.

While we have implemented industry-standard physical and cybersecurity measures, our network may still be vulnerable to unauthorized access, computer viruses, denial of service and other disruptive problems. Our Internet-based services may be interrupted as a result of the accidental or intentional actions of Internet users, our current and former employees or others. A party that is able to circumvent security measures could misappropriate proprietary information, attack our security and network system, and, perhaps, most importantly, cause interruptions in our operations. We have experienced in the past, and may experience in the future, security breaches and attacks. We may be required to expend

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significant capital or other resources to protect against the threat of security breaches and attacks or to alleviate problems caused by such actions. There can be no assurance that any measures implemented will not be circumvented in the future. Furthermore, a successful security breach or attack may lead us to incur substantial costs to repair damage or restore data, implement substantial organizational changes and training to prevent future similar attacks and lost revenues and litigation costs due to misused sensitive information, and cause substantial reputational damage.

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Our business is also vulnerable to delays or interruptions due to our reliance on infrastructure and related services provided by third parties. End-users of our offerings depend on ISPs and our system infrastructure for access to the Internet games and services we offer. Some of these services have experienced service outages in the past and could experience service outages, delays and other difficulties due to system failures, stability or interruption. For example, in February 2007, an earthquake off the coast of Taiwan, and in March 2011 an earthquake off the north-east coast of Japan, damaged several undersea fiber optic cables linking countries such as Malaysia, Singapore, Australia, Japan, South Korea, China, the United States and Europe, causing disruptions in Internet traffic worldwide. We may lose customers as a result of delays or interruption in service, including delays or interruptions relating to high volumes of traffic or technological problems, which may prevent communication over the Internet and could materially adversely affect our business, revenues, results of operations and financial condition.

### **Any failure to maintain a stable and efficient distribution and payment network could have a material and adverse impact on our Asian online game and service business, financial condition and results of operations**

Our Asian online game and service business operation relies heavily on a multi-layer distribution and payment network composed of third-party distributors for our sales to, and collection of payment from, our users. As we do not enter into long-term agreements with any of our distributors, we cannot assure you that we will continue to maintain favorable relationships with them. If we fail to maintain a stable and efficient distribution and payment network, our business, financial condition and results of operations could be materially and adversely affected.

In addition, our ability to process electronic commerce transactions depends on bank processing and credit card systems. In order to prepare for certain types of system problems, we have a formal disaster recovery plan. Nevertheless, any system failure, including network, software or hardware failure, which causes a delay or interruption in our e-commerce services could have a material adverse effect on our business, revenues, results of operations and financial condition.

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

A portion of our transactions are conducted through our websites. In such transactions, secured 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. In addition, we may face internal fraud, including potential unauthorized usage of customer credit card information by our employees. While we are not aware of any breaches of security on our websites having occurred and we have taken steps to prevent this, including the implementation of payment card industry data security standards, our current security measures may not be adequate. 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 and retain customers.

### **Undetected programming errors or defects in our software, services and games and the proliferation of cheating programs could materially and adversely affect our Asian online game and service business and the cloud computing business, financial condition and results of operations**

Our online games and cloud computing software and services may contain undetected programming errors or other defects. These errors or other defects could damage our reputation and subject us to liability. As to online games, parties unrelated to us may develop cheating programs that enable users to acquire superior features for their game characters that they would not have otherwise. Furthermore, certain cheating programs could cause the loss of a character's superior features acquired by a user. The occurrence of undetected errors or defects in our games, and our failure to discover and disable cheating programs affecting the fairness of our game environment, could disrupt our operations, damage our reputation and detract from the game experience of our users. As a result, such errors, defects and cheating programs could materially and adversely affect our business, financial condition and results of operations. If such errors, defects and cheating programs occur in software, services and games we operate, our business operations and, in turn, our business and financial condition, could be materially and adversely affected.

### **Operation of pirate game servers and the expenses incurred in protecting our Asian online game and service business operation against unlawful operations through pirate servers may adversely affect our business**

We face challenges from pirate game servers, which are game servers that operate unauthorized copies of our online games and permit users to play those games without purchasing pre-paid game cards from us. The existence of unauthorized servers may attract game players away from our games and may result in decreases in our revenues. Although we have made efforts to detect and shutdown pirate servers in Greater China, we cannot assure you that such efforts will be successful in eliminating these unauthorized servers. In addition, detailed comparisons of software codes and litigation proceedings are often necessary to enforce the intellectual property rights, whether owned by or licensed by us, which sometimes result in substantial costs. The continued illegal operation of any of our existing games by pirate game servers, or the illegal operation

of any of our new games by pirate servers, may materially and adversely affect our business, financial condition and results of operations.

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### **We may be subject to claims of intellectual property right infringement by third parties, which could subject us to significant liabilities and other costs**

Our success depends largely on our ability to use and develop our technology and know-how without infringing upon the intellectual property rights of third parties. We cannot ensure that third parties will not assert intellectual property claims against us. The validity and scope of claims relating to the intellectual property may involve complex scientific, legal and factual questions and analysis, and tend to be uncertain. If third parties assert copyright or patent infringement or violation of other intellectual property rights against us, we have to defend ourselves in legal or administrative proceedings, which can be costly and time consuming and may significantly divert the efforts and resources of our technical and management personnel. An adverse determination in any such proceedings to which we may become a party could subject us to significant liability to third parties, require us to seek licenses from third parties, and prevent us from selling our products and services. The imposition of liabilities that are not covered by insurance, in excess of insurance coverage or for which we are not indemnified by a content provider, could have a material adverse effect on our business, results of operations and financial condition.

### **We may need to incur significant expenses to protect our intellectual property rights, and if we are unable to adequately protect our intellectual property rights, our competitive position could be harmed**

We regard our copyrights, service marks, trademarks, trade secrets, patents and other intellectual property as critical to our success. We rely on a combination of copyright and trademark laws, trade secret protection, confidentiality and non-disclosure agreements, and other contractual provisions to protect our proprietary software, trade secrets and similar intellectual property. We have patents, copyrights and trademarks in certain jurisdictions and may apply for further trademark and copyright registrations and additional patents, which may provide such protection in relevant jurisdictions. However, we cannot assure you that our efforts will prove to be sufficient or that third parties will not infringe upon or misappropriate our proprietary rights. Unauthorized use of the intellectual property, whether owned by or licensed to us, could adversely affect our business and reputation.

The validity, enforceability and scope of protection of intellectual property in Internet-related industries are evolving, and therefore, uncertain. In particular, the laws and enforcement procedures of the PRC, Taiwan, and Hong Kong are uncertain or do not protect intellectual property rights to the same extent as the laws and enforcement procedures of the United States do. We may have to engage in litigation or other legal proceedings to enforce and protect our intellectual property rights, which could result in substantial costs and diversion of our resources, and have a material adverse effect on our business, financial condition and results of operations.

### **Our future results of operations or the growth of our business may suffer if we are unable to maintain satisfactory relationships with the licensors of our online games**

While we are focused on self-development of casual games, we have historically and may in the future source casual games, advanced casual games and MMOs through licensing from developers in various regions where online game development is relatively established. As of the date of this annual report, we have four licensed MMOs in our online game portfolio, including the games we currently offer and the games in the pipeline. We need to maintain stable and satisfactory working relationships with our licensors in order to ensure the continued operation of our licensed online games and our continued access to new online game licenses. We depend on our licensors to provide the necessary technical support for the operation of the licensed games as well as expansion packs and upgrades that sustain continuing interest in the games. Our ability to maintain satisfactory working relationships with our licensors may also influence our ability to license new online games developed by the same or other licensors. If we are unable to maintain satisfactory relationships with our licensors, our financial condition, results of operations, future profitability and growth prospects may be materially and adversely affected.

### **We may need additional capital in the future, and it may not be available on acceptable terms**

The development of our business may require significant additional capital in the future to:

fund our operations;

enhance and expand the range of products and services we offer; and

respond to competitive pressures and perceived opportunities, such as investment, acquisition and international expansion activities.

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We cannot assure you that additional financing will be available on terms favorable to us, if at all. If adequate funds are not available on acceptable terms, we may be forced to curtail or cease our operations. Moreover, even if we are able to continue our operations, any failure to obtain additional financing could have a material and adverse effect on our business, financial condition and results of operations, and we may need to delay the deployment of our services. See Item 5, Operating and Financial Review and Prospects B. Liquidity and Capital Resources.

### **We have had significant turnover in our management team and additional turnover could harm our business**

The success of our business is heavily dependent upon the services of our management team and other key personnel. We have experienced substantial turnover among members of our board of directors and senior management team in the past year. Further turnover of directors, senior management or key personnel could harm our business. Furthermore, we must successfully integrate all new management and other key personnel into our organization to achieve our operating objectives; failure to do so could adversely affect our business.

### **Our results of operations and financial condition are affected by political stability, as well as the occurrence of natural disasters and epidemics**

We operate our Asian online game and service business in Greater China. Political unrest, war, acts of terrorism and other instability, as well as natural disasters such as earthquakes and typhoons which are common in Greater China, can result in disruption to our business or the businesses of our customers.

Our business could be adversely affected by natural disasters and the effects of influenza A virus subtypes, such as H1N1 and H5N1, SARS or other epidemics. Any prolonged recurrence of such adverse public health developments in the regions where we operate may have material adverse effects on our business operations. These could include illness and loss of our management and key employees. Natural disasters or outbreak of epidemics may result in a decrease in economic activities or temporary closure of many businesses and disruption in our operations. 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.

### **We have a limited operating history in providing cloud computing services, which makes it difficult to predict our future operating results**

We introduced our first cloud computing services in early April 2013. As a result of our limited operating history, our ability to forecast our future operating results is limited and subject to a number of uncertainties, including our ability to plan for and model future growth. We face risks and uncertainties frequently experienced by growing companies in rapidly changing industries, such as the risks and uncertainties described herein. If our assumptions regarding these risks and uncertainties (which we use to plan our business) are incorrect or change due to changes in our markets, or if we do not address these risks successfully, our operating and financial results could differ materially from our expectations and our business could suffer.

### **The success of our cloud computing business is dependent on the growth and public acceptance of our services**

Our future success in cloud computing depends on our ability to significantly increase revenues generated from our services. In turn, the success of our cloud computing solutions and services depends, among other things, upon future demand for cloud-based communications systems and services. Because the use of our service requires that the user be a subscriber of an existing broadband Internet service, usually provided through a cable or digital subscriber line, or DSL, connection, slow or limited adoption of broadband Internet service could adversely affect the growth of our subscriber base and revenues. Although the number of broadband subscribers in Greater China has grown significantly over the last five years, cloud-based communications services have not yet been adopted by a majority of prospective business customers. To increase the deployment of broadband Internet services from broadband Internet service providers, telephone companies and cable companies must continue to invest in the deployment of high speed broadband networks to residential and business customers, over which we have no control. In addition, networks must improve quality of service for real-time communications, managing effects such as packet jitter, packet loss, and unreliable bandwidth, so that toll-quality service can be consistently provided. Cloud-based communications equipment and services must achieve a similar level of reliability that users of the public switched telephone network, or PSTN, have come to expect from their telephone service, and the cost and feature benefits of cloud-based communications must be sufficient to cause customers to switch away from traditional telephony service providers. We must devote substantial resources to educate customers and end users about the benefits of cloud-based communications solutions, in general, and our services in particular. Substantial, ongoing interaction with our customers in order to train and assist them with the deployment and use of our services over these networks is sometimes required. If any or all of these factors fail to occur, our business may be adversely affected.



**Our cloud computing business depends on continued and unimpeded access to the Internet by us and our users. Internet access providers and Internet backbone providers may be able to block, degrade or charge for access to or bandwidth use of certain of our products and services, which could lead to additional expenses and the loss of users**

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Our cloud computing solutions and services depend on the ability of our users to access the Internet, and certain of our products require significant bandwidth to work effectively. Currently, this access is provided by companies that have significant and increasing market power in the broadband and Internet access marketplace, including incumbent telephone companies, cable companies and mobile communications companies. Some of these providers offer products and services that directly compete with our own offerings, which give them a significant competitive advantage. Some of these providers have stated that they may take measures that could degrade, disrupt or increase the cost of user access to certain of our products by restricting or prohibiting the use of their infrastructure to support or facilitate our offerings, or by charging increased fees to us or our users to provide our offerings. While others, including some of the largest providers of broadband Internet access services, have committed to not engaging in such behavior, we cannot assure you that they will follow through on their commitments.

### **Intense competition in the markets in which we compete in cloud computing could prevent us from increasing or sustaining our revenue and increasing or maintaining profitability**

The cloud computing and telecommunications industries are highly competitive. We face intense competition from new cloud service providers, traditional telephone companies, wireless companies, cable companies, competitive local exchange carriers, alternative voice communication providers and independent VoIP providers.

Most of our current and potential competitors, particularly incumbent telephone and cable companies, have longer operating histories, significantly greater resources and name recognition, and a larger base of customers than we have. As a result, these competitors may have greater credibility with our existing and potential customers. They also may be able to adopt more aggressive pricing policies and devote greater resources to the development, promotion and sale of their products than we can to ours. Our competitors may also offer bundled service arrangements offering a more complete product despite the technical merits or advantages of our products. Competition could decrease our prices, reduce our sales, lower our gross profits or decrease our market share.

We also compete against established alternative voice communication providers and face competition from other large, well-capitalized Internet companies that have recently launched or plan to launch cloud-based services. In addition, we compete with independent cloud service providers. Some of these service providers may choose to sacrifice revenue in order to gain market share by offering their services at lower prices or for free. In order to compete with such service providers, we may have to significantly reduce our prices, which would affect our profitability.

We also are subject to the risk that new technologies may be developed that are able to deliver competing voice services at lower prices, better or more conveniently. Future competition from new technologies could have a material adverse effect on our growth and operating results.

Given the significant price competition in the markets for our products, we are at a significant disadvantage compared to many of our competitors, especially those with substantially greater resources, and therefore may be better able to withstand an extended period of downward pricing pressure. The adverse impact of a shortfall in our revenues may be magnified by our inability to adjust spending to compensate for such shortfall. Announcements of new products and technologies by our competitors or us could cause customers to defer purchases of our existing products, which also could have a material adverse effect on our business, financial condition or operating results.

### **The cloud computing market is subject to rapid technological change, and we depend on new product and service introductions in order to maintain and grow our business**

Cloud computing solutions and services is an emerging market that is characterized by rapid changes in customer requirements, frequent introductions of new and enhanced products, and continuing and rapid technological advancement. To compete successfully in this emerging market, we must continue to design, develop, manufacture, and sell new and enhanced cloud software products and services that provide increasingly higher levels of performance and reliability at lower cost.

### **Decreasing telecommunications rates and increasing regulatory charges may diminish or eliminate our competitive pricing advantage of our communications offerings, which yield significant savings over traditional phone systems**

Decreasing telecommunications rates may diminish or eliminate the competitive pricing advantage of our services, while increased regulation and the imposition of regulatory obligations could require us to either increase the retail price for our services, thus making us less competitive, or absorb such costs, thus decreasing our profit margins. International and domestic telecommunications rates have decreased significantly over the last few years in Greater China, and we anticipate these rates will continue to decline in all of the markets in which we do business or expect to do business. Users who select our services to take advantage of the current pricing differential between traditional telecommunications rates and our rates may switch to traditional telecommunications carriers if such pricing differentials diminish or disappear, however, and we will be unable to use such pricing differentials to attract new customers in the future. Continued rate decreases would require us to lower our rates to

remain competitive and would reduce or possibly eliminate any gross profit from our services. In addition, we may lose subscribers for our services.

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### **We rely on third-party network service providers to originate and terminate substantially all of our public switched telephone network calls**

We leverage the infrastructure of third-party network service providers to provide telephone numbers, PSTN call termination and origination services, and local number portability for our customers rather than deploying our own network throughout Taiwan. This decision has resulted in lower capital and operating costs for our business in the short term but has reduced our operating flexibility and ability to make timely service changes. If any of these network service providers cease operations or otherwise terminate the services that we depend on, the delay in switching our technology to another network service provider, if available, and qualifying this new service could have a material adverse effect on our business, financial condition or operating results.

While we believe that relations with our current service providers are good, and we have contracts in place, there can be no assurance that these service providers will be able or willing to supply cost-effective services to us in the future or that we will be successful in signing up alternative or additional providers. Although we could replace our current providers, if necessary, our ability to provide service to our subscribers could be impacted during this timeframe, and this could have an adverse effect on our business, financial condition or results of operations. The loss of access to, or requirement to change, the telephone numbers we provide to our customers also could have a material adverse effect on our business, financial condition or operating results.

Due to our reliance on these service providers, when problems occur in a network, it may be difficult to identify the source of the problem. The occurrence of hardware and software errors, whether caused by our service or another vendor's products, may result in the delay or loss of market acceptance of our products and any necessary revisions may force us to incur significant expenses. The occurrence of some of these types of problems may seriously harm our business, financial condition or operating results.

### **Our physical infrastructure is concentrated in a few facilities and any failure in our physical infrastructure or our inability to handle a growing number of simultaneous calls and other services could lead to significant costs and disruptions and could reduce our revenue, harm our business reputation and have a material adverse effect on our financial results**

Our leased network and data centers are subject to various points of failure. Problems with cooling equipment, generators, uninterruptible power supply, routers, switches, or other equipment, whether or not within our control, could result in service interruptions for our customers as well as equipment damage. Because our services do not require geographic proximity of our data centers to our customers, our infrastructure is consolidated into a few large facilities. Any failure or downtime in one of our data center facilities could affect a significant percentage of our customers. The total destruction or severe impairment of any of our data center facilities could result in significant downtime of our services and the loss of customer data. Because our ability to attract and retain customers depends on our ability to provide customers with highly reliable service, even minor interruptions in our service could harm our reputation. Additionally, in connection with the expansion or consolidation of our existing data center facilities from time to time, there is an increased risk that service interruptions may occur as a result of server relocation or other unforeseen construction-related issues.

We expect the volume of simultaneous calls to increase significantly as our subscriber base grows. Our systems may not be able to accommodate this additional volume. If we fail to maintain an appropriate level of operating performance, or if our service is disrupted, our reputation could be hurt and we could lose customers, all of which could have a material adverse effect on our business, financial condition or operating results.

Any future service interruptions could:

Cause our customers to seek damages for losses incurred;

Require us to replace existing equipment or add redundant facilities;

Affect our reputation as a reliable provider of hosting services;

Cause existing customers to cancel or elect to not renew their contracts; or

Make it more difficult for us to attract new customers.

Any of these events could materially increase our expenses or reduce our revenue, which would have a material adverse effect on our operating results.

**Increased energy costs, power outages, and limited availability of electrical resources may adversely affect our operating results**

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Our data centers are susceptible to increased costs of power and to electrical power outages. Our customer contracts do not contain provisions that would allow us to pass on any increased costs of energy to our customers, which could affect our operating margins. Any increases in the price of our services to recoup these costs could not be implemented until the end of a customer contract term. Further, power requirements at our data centers are increasing as a result of the increasing power demands of today's servers. Increases in our power costs could impact our operating results and financial condition. Since we rely on third parties to provide our data centers with power sufficient to meet our needs, our data centers could have a limited or inadequate amount of electrical resources necessary to meet our customer requirements. We attempt to limit exposure to system downtime due to power outages by using backup generators and power supplies. However, these protections may not limit our exposure to power shortages or outages entirely. Any system downtime resulting from insufficient power resources or power outages could damage our reputation and lead us to lose current and potential customers, which would harm our operating results and financial condition.

### **Dependence on network suppliers may adversely affect our operating results**

Our success depends in part upon the capacity, reliability, and performance of our network infrastructure, including the capacity leased from our Internet bandwidth suppliers. We depend on these companies to provide uninterrupted and error-free service through their telecommunications networks. Some of these providers are also our competitors. We exercise little control over these providers, which increases our vulnerability to problems with the services they provide. We have experienced and expect to continue to experience interruptions or delays in network service. Any failure on our part or the part of our third-party suppliers to achieve or maintain high data transmission capacity, reliability or performance could significantly reduce customer demand for our services and damage our business. As our customer base grows and their usage of telecommunications capacity increases, we will be required to make additional investments in our capacity to maintain adequate data transmission speeds, the availability of which may be limited or the cost of which may be on terms unacceptable to us. If adequate capacity is not available to us as our customers' usage increases, our network may be unable to achieve or maintain sufficiently high data transmission capacity, reliability or performance. In addition, our business would suffer if our network suppliers increased the prices for their services and we were unable to pass along the increased costs to our customers.

### **We depend on third-party vendors for mobile phones, IP phones, and video cameras, and any delay or interruption in manufacturing by these vendors would result in delayed or reduced shipments to our customers and may harm our business**

We rely on third-party vendors for mobile phones, IP phones, and video cameras to utilize our services. We currently do not have long-term supply contracts with any of these vendors. As a result, most of these third-party vendors are not obligated to provide products or perform services to us for any specific period, in any specific quantities or at any specific price, except as may be provided in a particular purchase order. The inability of these third-party vendors to deliver IP phones of acceptable quality and in a timely manner, particularly the sole source vendors, could adversely affect our operating results or cause them to fluctuate more than anticipated. Additionally, some of our products may require specialized or high-performance component parts that may not be available in quantities or in time frames that meet our requirements.

### **Potential infringement on third-party intellectual property rights could disrupt our business**

There has been substantial litigation in the communications, VoIP services, semiconductor, electronics, and related industries regarding intellectual property rights and, from time to time, third parties may claim infringement by us of their intellectual property rights. Our broad range of current technology, including IP telephony systems, digital and analog circuits, software, and semiconductors, increases the likelihood that third parties may claim infringement by us of their intellectual property rights.

Certain technologies necessary for us to provide our services may, in fact, be patented by other parties either now or in the future. If such technology were held under patent by another person, we would have to negotiate a license for the use of that certain technology. We may not be able to negotiate such a license at a price that is acceptable. The existence of such patents, or our inability to negotiate a license for any such technology on acceptable terms, could force us to cease using such technology and offering products and services incorporating such technology. If we were found to be infringing on the intellectual property rights of any third party in lawsuits or other claims and proceedings that may be asserted against us in the future, we could be subject to liabilities for such infringement, which could be material. We could also be required to refrain from using, manufacturing or selling certain products or using certain processes, either of which could have a material adverse effect on our business and operating results. From time to time, we may receive in the future, notices of claims of infringement, misappropriation or misuse of other parties' proprietary rights. There can be no assurance that we will prevail in these discussions and actions or that other actions alleging infringement by us of third-party patents will not be asserted or prosecuted against us. Furthermore, lawsuits like these may require significant time and expense to defend, may divert management's attention away from other aspects of our operations and, upon resolution, may have a material adverse effect on our business, results of operations, financial condition and cash flows.

### **We may need to incur significant expenses to protect our intellectual property rights, and if we are unable to adequately protect our intellectual property rights, our competitive position could be harmed**



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We regard our copyrights, service marks, trademarks, trade secrets, patents and other intellectual property as critical to our success. We rely on a combination of copyright and trademark laws, trade secret protection, confidentiality and non-disclosure agreements, and other contractual provisions to protect our proprietary software, trade secrets and similar intellectual property. We have patents, copyrights and trademarks in certain jurisdictions and may apply for further trademark and copyright registrations and additional patents, which may provide such protection in relevant jurisdictions. However, we cannot assure you that our efforts will prove to be sufficient or that third parties will not infringe upon or misappropriate our proprietary rights. Unauthorized use of the intellectual property, whether owned by or licensed to us, could adversely affect our business and reputation.

The validity, enforceability and scope of protection of intellectual property in Internet-related industries are evolving, and therefore, uncertain. In particular, the laws and enforcement procedures of Taiwan and Hong Kong generally do not protect intellectual property rights to the same extent as the laws and enforcement procedures of the United States. We may have to engage in litigation or other legal proceedings to enforce and protect our intellectual property rights, which could result in substantial costs and diversion of our resources, and may have a material adverse effect on our business, financial condition and results of operations.

### **Our ability to offer services outside Taiwan is subject to different local regulatory environments, which may be unknown, complicated and uncertain**

Regulatory treatment of cloud computing solutions and services outside Taiwan varies from country to country and often the applicable laws are unclear. We plan to distribute our products and services directly to consumers and through resellers that may be subject to telecommunications regulations in their home countries. Any failure by us or our customers and resellers to comply with these laws and regulations could reduce our revenue and profitability. Some countries may require us to register as a telecommunications provider based on our relationship with local resellers and may subject us to fines or penalties should we fail to do so. In addition, some countries are considering subjecting cloud-based communications services to the regulations applied to traditional telephone companies. Regulatory developments such as these could have a material adverse effect on the use of our services in international locations.

### **The rates we pay to underlying telecommunications carriers may increase which may reduce our profitability and increase the retail price of our service**

New rules in Taiwan may impact charges that regulated telecommunications carriers assess each other for originating and terminating traffic. It is possible that new rules will subject cloud-based communications traffic to increased charges. Should this occur, the rates that we pay to our underlying carriers may increase which may reduce our profitability and may also increase the retail price of our service, making our service less competitive with other providers of similar calling services.

### **We could be liable for breaches of security on our web site, fraudulent activities of our users, or the failure of third-party vendors to deliver credit card transaction processing services**

A fundamental requirement for operating an Internet-based, international communications service and electronically billing our customers is the secure transmission of confidential information and media over public networks. Although we have developed systems and processes that are designed to protect consumer information and prevent fraudulent credit card transactions and other security breaches, failure to mitigate such fraud or breaches may adversely affect our operating results. The law relating to the liability of providers of online payment services is currently unsettled and certain jurisdictions may enact their own rules with which we may not comply. We rely on third-party providers to process and guarantee payments made by our subscribers up to certain limits, and we may be unable to prevent our customers from fraudulently receiving goods and services. Our liability risk will increase if a larger fraction of our transactions involve fraudulent or disputed credit card transactions. Any costs we incur as a result of fraudulent or disputed transactions could harm our business. In addition, the functionality of our current billing system relies on certain third-party vendors delivering services. If these vendors are unable or unwilling to provide services, we will not be able to charge for our services in a timely or scalable fashion, which could significantly decrease our revenue and have a material adverse effect on our business, financial condition and operating results.

### **We may experience losses due to subscriber fraud and theft of service**

Subscribers may in the future obtain access to our service without paying for monthly service and international toll calls by unlawfully using our authorization codes or by submitting fraudulent credit card information. To date, such losses from unauthorized credit card transactions and theft of service have not occurred. We have implemented anti-fraud procedures in order to control losses relating to these practices, but these procedures may not be adequate to effectively limit all of our exposure in the future from fraud. If our procedures are not effective, consumer fraud and theft of service could significantly decrease our revenue and have a material adverse effect on our business, financial condition and operating results.



**A high rate of customer terminations would negatively affect our business by reducing our revenue or requiring us to spend more money to grow our customer base**

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We could experience a high customer termination, or churn, rate in the future if customers are not satisfied with our service. Other factors, including increased competition from VoIP providers, alternative technologies, and adverse business conditions may also influence our churn rate.

Because of churn, we have to acquire new customers on an ongoing basis just to maintain our existing level of customers and revenues. As a result, marketing expenditures are an ongoing requirement of our business. If our churn rate is high and increases, we will have to acquire even more new customers in order to maintain our existing revenues. We incur significant costs to acquire new customers, and those costs are an important factor in determining our net profitability. Therefore, if we are unsuccessful in retaining customers or are required to spend significant amounts to acquire new customers beyond those budgeted, our revenue could decrease and our net income could decrease.

### **We need to retain key personnel to support our products and ongoing operations**

The development and marketing of our cloud-based communications and services will continue to place a significant strain on our limited personnel, management, and other resources. Our future success depends upon the continued services of our executive officers and other key employees who have critical industry experience and relationships that we rely on to implement our business plan. None of our officers or key employees is bound by employment agreements for any specific term. The loss of the services of any of our officers or key employees could delay the development and introduction of, and negatively impact our ability to sell our services which could adversely affect our financial results and impair our growth. We currently do not maintain key person life insurance policies on any of our employees.

### **We have outstanding receivables from the disposal of Infocomm Asia Holdings Pte. Ltd. and Spring Asia Limited**

On July 2, 2012 GigaMedia Asia Pacific Limited ( GigaMedia Asia ), IAH, Management Capital International Limited ( MCIL ), and Roland Ong Toon Wah ( ROTW ) entered into a series of agreements whereby GigaMedia Asia agreed to sell to MCIL 1,463,930 Class A shares of IAH (representing 6.48% of the issued and outstanding shares of IAH), 1,208,881 Class B shares of IAH (representing 53.52% issued and outstanding shares) (the IAH Share Purchase Agreement ), and to IAH 100% of the shares in Spring Asia Limited ( Spring Asia ) held by GigaMedia through IAH (the Spring Asia Share Purchase Agreement ). The total purchase price was US\$3 million for the Spring Asia shares, and US\$1.00 for the IAH shares, excluding taxes. All consideration for the Spring Asia shares was to be paid in four equal installments of US\$750,000 over a nine-month period. The parties also executed other ancillary agreements on the same date, including a Shareholders Agreement (among MCIL, GigaMedia Asia, ROTW and IAH, the IAH Shareholders Agreement ), a Share Charge Agreement (between IAH and GigaMedia Asia), and an Escrow Agreement (among IAH, GigaMedia Asia and Trident Trust Company (Singapore) Pte. Limited). As of April 12, 2013, IAH had defaulted on its second, third, and fourth payments in the total amount of US\$2.25 million. We have provided sufficient notice and proper instructions to the escrow agent for us to re-possess Spring Asia shares proportionate to IAH's defaults.

We entered into a Settlement Agreement, dated April 17, 2013, with IAH, MCIL, Spring Asia and ROTW (the IAH Settlement Agreement ), whereby IAH and/or ROTW agreed to pay us the outstanding Spring Asia purchase price of US\$2.25 million, plus interest of US\$8,390, within 15 days after the date of the IAH Settlement Agreement. Upon full payment of the purchase price and interest by IAH and/or ROTW, GigaMedia Asia will release and transfer the Spring Asia shares repossessed by GigaMedia Asia to IAH and/or ROTW.

Additionally, under the IAH Settlement Agreement, MCIL exercised its call option pursuant to the IAH Share Purchase Agreement to purchase all of the remaining 451,830 IAH shares held by us at a purchase price of US\$1 million. The entire US\$1 million purchase price is due on May 2, 2013.

### **Risks Related to Doing Business in Greater China**

**There are currently no clear laws or regulations governing virtual asset property rights, in particular, in Greater China, and therefore, it is not clear what liabilities, if any, online game operators may have in respect of virtual assets**

In the course of playing online games, some virtual assets, such as special equipment, player experience grades and other features of our users game characters, are acquired and accumulated. Such virtual assets can be important to online game players. In practice, virtual assets can be lost for various reasons, often through unauthorized use of user identifications by other users and occasionally through data loss caused by delay of network service or by a network crash. Currently there are no clear laws or regulations governing virtual asset property rights, in particular, in Greater China where we operate our Asian online game and service business. As a result, it is unclear under PRC law whether an operator of online games such as us would have any liability (whether in contract, tort or otherwise) for loss of such virtual assets by game players. Based on several judgments regarding the liabilities of online game operators for loss of virtual assets by game players, the PRC courts have generally required online game operators to provide well-developed security systems to protect such virtual assets owned by game players. In the case of a loss of virtual assets, we may be sued by online game players and could be held liable for damages, which may negatively affect our business,

financial condition and results of operations.

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### **There are economic risks associated with doing business in Taiwan, particularly due to the tense relationship between Taiwan and the PRC**

Our principal executive offices and a significant portion of our assets are located in Taiwan and a major portion of our revenues of Asian online game and service business are derived from our operations in Taiwan. Taiwan, as part of the Republic of China, has a unique international political status. The PRC asserts sovereignty over mainland China and Taiwan and does not recognize the legitimacy of the Taiwan government. Relations between Taiwan and the PRC and other factors affecting the political or economic conditions of Taiwan could also affect our Asian online game and service and GigaCloud businesses.

### **Risks Related to Ownership of our Shares**

#### **The price of our Shares has been volatile historically and may continue to be volatile, which may make it difficult for holders to resell our Shares when desired or at attractive prices**

The trading price of our Shares has been and may continue to be subject to wide fluctuations. In 2012, the closing prices of our Shares on the Nasdaq Stock Market have ranged from US\$0.81 to US\$1.48 per share, and the closing price on March 29, 2013 was US\$1.05. Our Share price may fluctuate in response to a number of events and factors. In addition, the financial markets in general, and the market prices for Internet-related companies in particular, have experienced extreme volatility that often has been unrelated to the operating performance of such companies. These broad market and industry fluctuations may adversely affect the price of our Shares, regardless of our operating performance.

#### **Our Shares are listed on the Nasdaq Global Market and if we fail to meet the standards for continued listing of our Shares on Nasdaq, the Shares could be delisted from the Nasdaq Stock Market**

Our Shares are listed on the Nasdaq Global Market. The Nasdaq Global Market has several quantitative and qualitative requirements companies must comply with to maintain listing, including a US\$1.00 minimum bid price per share. The trading prices for our Shares in the year 2012 were around the US\$1.00 range and traded below US\$1.00 several times. As of March 29, 2012, the closing price for our Shares was US\$1.05.

There can be no assurance that we will continue to meet all of the requirements for continued Nasdaq listing. If we fail to comply with the minimum bid price requirement, our Shares could be delisted from Nasdaq, which could have a material adverse effect on our stock prices and our standing with current and future investors.

#### **We are controlled by the Koo family, which has significant influence in determining the outcome of any corporate transaction or other matters submitted to our shareholders for approval, and their interests may conflict with your interests**

As of March 29, 2013, a member of the Koo family beneficially owned approximately 21.29 percent of our outstanding Shares. Accordingly, a member of the Koo family has significant influence in determining the outcome of any corporate transaction or other matters submitted to our shareholders for approval, including mergers, consolidations, the sale of all or substantially all of our assets and the power to prevent or cause a change in control. The interests of such member of the Koo family may differ from or conflict with your interests.

#### **Our transactions with related parties may not benefit us and may harm our Company**

We have entered into several transactions with certain related parties. We believe that we have conducted our related-party transactions on an arm's-length basis and on terms comparable to, or more favorable to us than, similar transactions we would enter into with independent third parties. However, we cannot assure you that all our future transactions with related parties will be beneficial to us. See Item 7, Major Shareholders and Related-Party Transactions in this annual report.

#### **The ability of our subsidiaries in Taiwan to distribute dividends to us may be subject to restrictions under the laws of Taiwan**

We are a holding company, and some of our assets constitute our ownership interests in our subsidiaries in Taiwan, including Hoshin GigaMedia, which owns the Taiwan-based operations of our Asian online game and service business. Accordingly, part of our primary internal source of funds to meet our cash needs is our share of the dividends, if any, paid by our subsidiaries, including those in Taiwan. The distribution of dividends to us from these subsidiaries in Taiwan is subject to restrictions imposed by the applicable corporate and tax regulations in these countries, which are more fully described in Item 5, Operating and Financial Review and Prospects B. Liquidity and Capital Resources Dividends from Our Subsidiaries in this annual report. In addition, although there are currently no foreign exchange control regulations which restrict the ability of our subsidiaries in Taiwan to distribute dividends to us, the relevant regulations may be changed and the ability of these subsidiaries to distribute dividends to us may be restricted in the future.



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### **Anti-takeover provisions under the Singapore Securities and Futures Act (Chapter 289) and the Singapore Code on Take-overs and Mergers may delay, deter or prevent a future takeover or change of control of our Company, which could adversely affect the price of our Shares**

The Singapore Code on Take-overs and Mergers (the Code), issued pursuant to Section 321 of the Singapore Securities and Futures Act (Chapter 289) regulates the acquisition of ordinary shares of, inter alia, listed public companies and contains certain provisions that may delay, deter or prevent a future takeover or change of control of our Company. Any person acquiring an interest, either on his own or together with parties acting in concert with him, in 30 percent or more of the voting shares in our Company must, except with the prior consent of the Singapore Securities Industry Council (the SIC), extend a takeover offer for the remaining voting shares in our Company in accordance with the provisions of the Code. Likewise, any person holding between 30 percent and 50 percent of the voting shares in our Company, either on his own or together with parties acting in concert with him, must, except with the prior consent of the SIC, make a takeover offer in accordance with the provisions of the Code if that person together with parties acting in concert with him acquires additional voting shares in excess of one percent of the total number of voting shares in any six-month period.

Under the Code, an offeror must treat all shareholders of the same class in an offeree company equally. A fundamental requirement is that shareholders in the company subject to the takeover offer must be given sufficient information, advice and time to consider and decide on the offer.

These provisions contained in the Code may discourage or prevent transactions that involve an actual or threatened change of control of our Company. This may harm you because an acquisition bid may allow you to sell your Shares at a price above the prevailing market price.

### **Our shareholders may be subject to Singapore taxes**

Singapore tax law may differ from the tax laws of other jurisdictions, including the United States. Gains from the sale of our Shares by a person not tax resident in Singapore may be taxable in Singapore if such gains are part of the profits of any business carried on in Singapore. For additional information, see Item 10, Additional Information E. Taxation Singapore Tax Consideration in this annual report. You should consult your tax advisors concerning the overall tax consequences of acquiring, owning or selling the Shares.

### **We are a Singapore company, and because the rights of shareholders under Singapore law differ from those under U.S. law, you may have difficulty in protecting your shareholder rights or enforcing any judgment obtained in the U.S. against us or our affiliates**

Our corporate affairs are governed by our memorandum and articles of association and by the applicable laws governing corporations incorporated in Singapore. The rights of our shareholders and the responsibilities of members of our board of directors under Singapore law are different from those applicable to a corporation incorporated in the United States and, therefore, our shareholders may have more difficulty protecting their interests in connection with actions by the management, members of our board of directors or our controlling shareholders than they would as shareholders of a corporation incorporated in the United States.

Our Company is incorporated under the laws of the Republic of Singapore. Many of our directors and senior management reside outside the United States. As a result, it may be difficult for investors to effect service of process within the United States upon us or any of these persons or to enforce in the United States any judgment obtained in the U.S. courts against us or any of these persons, including judgments based upon the civil liability provisions of the U.S. federal securities laws or any state or territory of the United States. Judgments of the U.S. courts based upon the civil liability provisions of the U.S. federal securities laws may not be enforceable in Singapore courts, and it is unclear whether Singapore courts will enter judgments in original actions brought in Singapore courts based solely upon the civil liability provisions of the U.S. federal securities laws.

### **We may be deemed to be an investment company under the United States Investment Company Act of 1940, which could have a significant negative impact on our results of operations**

We may be deemed to be an investment company under the United States Investment Company Act of 1940 (the 1940 Act), and may suffer adverse consequences as a result. Generally, the 1940 Act provides that a company is an investment company if the company (i) is, holds itself out as or proposes to be engaged primarily in the business of investing, reinvesting or trading in securities or (ii) is engaged or proposes to engage in the business of investing, reinvesting, owning, holding or trading in securities and owns or proposes to acquire investment securities having a value exceeding 40% of the value of its total assets (exclusive of U.S. government securities or cash items) on an unconsolidated basis. Under the 1940 Act, investment securities include, among other things, securities of non-majority owned businesses. However, a company that is primarily engaged, directly or through wholly-owned subsidiaries, in a business or businesses other than that of investing, reinvesting, owning, holding or trading in securities is not an investment company.



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In the past, we disposed of our online gambling business and made several significant investments in online game developers and operators. As a result of these transactions, we have a significant amount of cash and securities. See Item 4, Information on the Company B. Business Overview

Gaming Software and Service Business for additional information. Consequently, there is a risk that we could be deemed to be an investment company because our investment securities may be deemed to comprise more than 40% of our total assets (exclusive of U.S. government securities or cash items) on an unconsolidated basis pending investment of disposal proceeds into our businesses.

However, based on our historical and current business activities, our intentions, the manner in which we hold ourselves out to the public, the primary activities of our officers and directors and an analysis of our non-cash assets and income during 2012, the first quarter of 2013 and in prior periods, we believe that the better view is that we are not an investment company. Nevertheless, a part of the determination of whether we are an investment company is based upon the composition and value of our non-cash assets, a significant portion of which are presently comprised of our Strategic Investments. As a result, we could be deemed to be an investment company.

We intend to continue to conduct our businesses and operations so as to avoid being required to register as an investment company. We have sought opportunities to deploy our capital in a manner which would result in the Company acquiring majority interests in entities or businesses that complement or enhance our remaining businesses or would otherwise assist the Company in achieving our current corporate objectives. We have also limited, and intend to continue to limit, new Strategic Investments to those opportunities which would present excellent opportunities to complement or enhance our remaining businesses or would otherwise assist the Company in achieving our current corporate objectives. If, nevertheless, we were to be required to register as an investment company, because we are a foreign company, the 1940 Act would prohibit us and any person deemed to be an underwriter of our securities from offering for sale, selling or delivering after sale, in connection with a public offering, any security issued by the Company in the United States. Additionally, we may be unable to continue operating as we currently do and might need to acquire or sell assets that we would not otherwise acquire or sell in order to avoid being treated as an investment company as defined under the 1940 Act. We may incur significant costs and management time in this regard, which could have a significant negative impact on our results of operations.

### **We may be classified as a passive foreign investment company for U.S. federal income tax purposes. As a result, you may be subject to materially adverse tax consequences with respect to Shares**

In light of our significant cash balances and portfolio of investment securities, we believe that it is likely that we were classified as a passive foreign investment company, or PFIC, for the taxable year ended December 31, 2012, and we will likely be a PFIC for our current taxable year ending December 31, 2013, unless our share value increases and/or we invest a substantial amount of the cash and other passive assets we hold in assets that produce or are held for the production of non-passive income. In addition, it is possible that one or more of our subsidiaries may be or become classified as a PFIC for U.S. federal income tax purposes. A non-United States corporation, such as us, will be classified as a PFIC for any taxable year in which 75 percent or more of its gross income consists of certain types of passive income or 50 percent or more of the average quarterly value of its assets (as generally determined on the basis of fair market value) during such year produce or are held for the production of passive income. For this purpose, cash and other assets readily convertible into cash are generally classified as passive and goodwill and other unbooked intangibles associated with active business activities may generally be classified as non-passive.

If we were to be classified as a PFIC in any taxable year during which a U.S. person (as defined in E. Taxation U.S. Tax Considerations Passive Foreign Investment Company ) holds our Shares, such U.S. person may incur significantly increased United States income tax on gain recognized on the sale or other disposition of the Shares and on the receipt of distributions on the Shares to the extent such gain or distribution is treated as an excess distribution under the U.S. federal income tax rules. Furthermore, a U.S. person will generally be treated as holding an equity interest in a PFIC in the first taxable year of the U.S. Person's holding period in which we become a PFIC and subsequent taxable years ( PFIC-Tainted Shares ) even if, in fact, cease to be a PFIC in subsequent taxable years. Accordingly, a U.S. person, who acquires our Shares during the current taxable year ending 2013 or subsequent taxable years, should, to the extent an election is available, consider making a mark-to-market election in the first taxable year of such holder's holding period to avoid owning PFIC-Tainted Shares. For more information, see the section entitled E. Taxation U.S. Tax Considerations Passive Foreign Investment Company .

### **Fluctuations in the exchange rates between the U.S. dollar and other currencies in which we conduct our business could adversely affect our profitability**

The operations of our Asian online game and service business are conducted in NT dollars and Hong Kong dollars. Accordingly, fluctuations in the exchange rates could have a positive or negative effect on our reported results. Generally, an appreciation of NT dollars or Hong Kong dollars against U.S. dollars results in a foreign exchange loss for monetary assets denominated in U.S. dollars, and a foreign exchange gain for monetary liabilities denominated in U.S. dollars. On the contrary, a devaluation of NT dollars, Hong Kong dollars, or Singapore dollars against U.S. dollars results in a foreign exchange gain for monetary assets denominated in U.S. dollars, and a foreign exchange loss for monetary liabilities denominated in U.S. dollars. Given the constantly changing currency exposures and the substantial volatility of currency exchange rates, we cannot predict the effect of exchange rate fluctuations upon future operating results. There can be no assurance that we will not



experience currency losses in the future, which could have a material adverse effect on our business, revenues, results of operations and financial condition.

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### **ITEM 4. INFORMATION ON THE COMPANY**

#### **A. History and Development of Our Company**

Our business was founded as Hoshin GigaMedia in October 1998 and we began offering broadband Internet access and services in Taiwan. For the purpose of a public equity offering, GigaMedia Limited was incorporated in Singapore in September 1999 as a company limited by shares. We acquired 99.99 percent of equity interest in Hoshin GigaMedia in November 1999 and the remaining 0.01 percent in October 2002.

In February 2000, we completed the initial public offering of our Shares. Our Shares are traded on the NASDAQ Stock Market under the symbol GIGM.

In January 2006, with a view to developing a diversified portfolio of growth businesses, we acquired FunTown, an Asian online game and service business operated in Taiwan and Hong Kong. In 2012, we began internal development of GigaCloud, a cloud computing software business focused on serving SMEs in Greater China. GigaCloud completed development of its first bundle of software and services in March 2013 and began commercial operations in April 2013.

As part of plans to turn around the Company's financial performance, in 2012 we began implementation of a disposal and asset optimization program targeting non-strategic investments and underperforming assets. In the second quarter of 2012, we closed our loss-making online game operations in Shanghai, and initiated the disposal of underperforming online game operations in Singapore. In the second quarter of 2013, we expect to complete the disposal of our Singapore operations and continued to dispose of non-strategic game studio holdings. We also completed the sale of our remaining 33.66 percent interest in the underperforming legacy online gambling operations of Everest Gaming in 2012.

Descriptions of our principal capital expenditures and divestitures and descriptions of acquisitions of material assets are found in our discussion and analysis of financial condition and results of operation and in the notes to our consolidated financial statements included elsewhere in this annual report. See Item 5, Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 .

There have been no public takeover offers by third parties in respect of our shares or by us in respect of other companies' shares which have occurred during the last and current financial year.

Our Singapore company registration number is 199905474H. Our principal executive offices are located at 8F, No. 22, Lane 407, Section 2, Tiding Boulevard, Taipei, Taiwan, and our telephone number is 886-2-2656-8000. Our website address is: <http://www.gigamedia.com> . Our agent in the U.S. is Computershare Limited and its office address is located at 480 Washington Blvd. Jersey City, the United States.

#### **B. Business Overview**

We are a diversified growth business with online game operations in Taiwan, Hong Kong and Macau and a cloud computing software and services business based in Taipei.

We own 100 percent of and operate FunTown, a leading online game portal in Taiwan and Hong Kong. FunTown is focused on the high-growth mobile and browser-based casual games market in Asia.

We also own 100 percent of and operate GigaCloud, a provider of cloud computing solutions and related services focused on the emerging cloud services market for SMEs in Greater China.

#### **Online Games Business**

##### ***Overview***

FunTown is focused on the high-growth mobile and browser-based casual games market in Asia. FunTown has a strong track record of developing and monetizing PC-based casual games, including by revenues one of the largest MahJong offerings in Taiwan, and we plan to leverage that as we restructure the business and extend our offerings to mobile and browser-based games in select areas and geographies going forward.



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Most of our games are operated or expected to be operated under the item-billing revenue model ( Item-Billing ). Under the Item-Billing model, users are able to access the basic functions of a casual online game for free. Players may choose to purchase in-game value-added services as well as in-game virtual items and premium features to enhance the game experience. These services and items allow players to utilize more functions, improve performance and skills, and personalize the appearance of a game character. Game points are consumed as users purchase value-added services and in-game items.

We have experienced seasonality in the form of slower sales of FunTown's online game and service business in the second and third quarters, during which people tend to spend less time indoors and online as daylight hours increase and the weather conditions improve. Typically, our first and fourth quarters have been our strongest revenue periods.

To complement our offerings and strengthen their appeal, we focus on building community-based online platforms that cater to different social networking needs of our users and provide various channels to facilitate communications among them.

We intend to continue to seek growth and enhance our market position in the online games industry by increasing focus on mobile and browser-based social casino games and expect to drive growth both organically and via mergers and acquisitions.

### ***Our Games***

Our portfolio of online games includes predominantly PC-based, non-cash gambling or casino casual games, including MahJong and various card and table games. FunTown's offers over 30 PC-based non-cash gambling or casino casual games and two MMOs. We have also launched an MahJong game application which uses a browser or web-based technology with no download required.

#### ***MahJong***

MahJong is a traditional and highly popular Chinese tile game, which is widely played in Taiwan, Hong Kong, the PRC, Japan, South Korea and many other Asian regions. Similar to poker, MahJong involves skill, strategy, calculation, as well as a certain degree of chance.

Through our FunTown-branded platform, we develop and offer various local versions of MahJong for players in Asia, particularly for those from Taiwan and Hong Kong. To play our online MahJong games, players install the client-end software which can be downloaded free of charge from our game websites. Players can compete with anyone throughout the FunTown network. Our MahJong games are designed for players of all levels of skill and experience. To accommodate various needs of players, we offer different online MahJong rooms based on skill levels or stakes. We believe our online MahJong game site is one of the largest online MahJong networks in Taiwan.

Players may play our online MahJong free of charge. To continue to play on a regular basis and establish a track record inside our online MahJong community, players may choose to purchase game points or game-playing time through various distribution channels, such as convenience stores and computer-based payment processing terminals. By purchasing our game points, players may exchange for virtual currency and deposit into their virtual bank accounts. The virtual currency may be used to play MahJong and other games in the FunTown game site or to purchase in-game virtual items, but may not be redeemed for cash.

Our PC-based MahJong offering faced strong competition in 2012 from the growth of mobile and browser-based online games, driven by the popularity of social networks and high mobile device usage in our markets. We responded by launching in February 2013 our MahJong game application which uses a web or browser-based technology with no download required. This simplified user sign-in procedures and enabled tighter integration with social networking platforms by allowing users to log into our game directly via their accounts at the social networking platform. We also launched our MahJong product on the iPad platform in May 2012.

We organize offline events from time to time with a view to attract more players and enhance our leading position in the online MahJong market.

#### ***Non-cash Gambling or Casino Casual Games***

Through our FunTown-branded platform, we offer various non-cash gambling or casino casual games. These online games are Internet-based and developed through computer simulation and adaptation of non-computer games, which are traditionally played offline. The FunTown platform targets players from different regions, particularly Taiwan and Hong Kong.



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We provide many different online card games, which are popular in various regions in Asia. Players can select their desired table based on the level of skill or stakes. These games are designed with online multiplayer features that allow players to compete against one another. We also offer chance-based games, including bingo, lotto, horse racing, Sic-Bo, slots and various simple casual games.

Like online MahJong, players may play our FunTown games for free. They may choose to purchase playing time or virtual currency to play on a continuous and regular basis. Virtual currencies may be used to play all the games in the FunTown game site or to purchase virtual items, but may not be redeemed for cash.

### *MMOs*

In Taiwan and Hong Kong, we offer two MMOs through FunTown. In June 2006, we launched the MMO Tales Runner. Tales Runner is a multi-player obstacle running game in which players compete by running, jumping, dashing and using items. Since the launch, Tales Runner has become one of the most popular online sports games in Hong Kong. In November 2010, we commercially launched in Taiwan, Hong Kong and Macau the MMO game Alliance of Valiant Arms, an online first person shooting game which provides large-scale and team-based combat.

Players download and install client software from our websites, except for browser-based games, where players can play directly from a web browser. Our MMOs are offered free-of-charge to all players. In order to enhance their online game playing experience, players may purchase virtual items that enhance their characters' performance and game playing experience, or personalize their characters.

In October 2010, we acquired a non-controlling interest in XLGames, an online game developer in Korea, through an investment in XLGames. As a result of the transaction, we received certain strategic rights, including exclusive rights to operate the MMO game ArchAge in Taiwan, Hong Kong, and Macau. XLGames launched the game in Korea in January 2013. As of March 31, 2013, GigaMedia has not scheduled the launch of ArchAge in its markets.

### *Game Sources*

#### *In-house development of Non-cash Gambling or Casino Casual Games*

We develop the gambling or casino games offered on FunTown's game platform, including online MahJong, card games, and other simple casual games. Our in-house development enables us to have better control of the game features and allow for seamless integration into our FunTown platform. In order to support product development capabilities and develop our proprietary online games, we intend to expand our Web-based social games development capabilities. As of March 31, 2013, we have an in-house development team comprised of approximately 66 software and design engineers.

#### *Sources of MMOs*

Our focus is on casual games. However, historically we have sourced MMOs through licensing from developers in various regions where online game development is well established. We monitor each of the United States, South Korean, the PRC, Japanese, Southeast Asia and European markets and maintain communications with a number of leading game development studios to identify and source new online games.

In selecting games, we evaluate the key factors that indicate the market trend and player demand and interest in the regions where we operate. We believe that our market analysis enables us to better assess the quality, risks, costs and potential returns of the games.

Prior to negotiating a license agreement with a game developer, our game testing team evaluates the game and prepares detailed evaluation reports covering the theme, storyline, in-game culture and environment, character progression, system architecture, game art, design, virtual articles and items.

Based on the results of our evaluation, we may at times enter into a license agreement to operate select games. The cost of licensing games from developers generally consists of an upfront licensing fee, which we normally pay in several installments, and ongoing licensing fees, or royalties, which are equal to a percentage of revenues generated from operation of the game. We may also have to provide certain minimum guarantees in royalties to developers.

In preparing for the commercial launch of each new game, we cooperate with the game developer to localize the game to make it suitable for the target markets where we plan to launch. Once the developer completes the localization and provides the first-built version, we conduct closed beta testing of the game with a select group of users. During the test period, we identify and eliminate any technical problems, assess how likely

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users will be to play the game regularly over a period of time (referred to as user stickiness ), and modify and add certain game features in order to increase user stickiness. The closed beta testing is followed by open beta testing, during which we operate our games under open market conditions and monitor the performance, consistency and stability of operational systems for the game.

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Following the commercial launch of a game, we regularly implement improvements and upgrades to our games.

### ***Fun Town Platform and Services***

Our FunTown platform provides many online game services for the users to enhance their playing and entertainment experiences, facilitate information communication among them and support the development of a strong player community. These services include:

**Player Clubs.** FunTown offers online club services in its game community. FunTown players can form their own clubs, invite other players with similar interests or skill levels to join, and organize online and offline events for club members. Player clubs complement the strong social features of online games by helping to maintain an online game community.

**Tournaments.** FunTown provides various tournaments for its online MahJong players. After players join a club, they can participate in biweekly online inter-club tournaments. On an annual basis, FunTown organizes large-scale tournaments, in which a large number of players are invited to the tournament premises and compete online via computers.

**Avatars.** To enhance players' overall entertainment experience, FunTown offers many in-game virtual items which may be purchased by players to customize their online personal graphic profiles, or avatars. Players use avatars to create their own unique look while participating in the online community. The virtual items for avatars include facial expressions, clothes and different accessories. These items are particularly popular with younger players, who customize their avatars to establish unique identities and pursue distinct fashions in the online community.

**Friends and Family Messenger.** The FunTown platform has a unique function designed for players' personal contacts, which is similar to the contact list of instant message programs. This enables players to see when their friends and family members are online and invite people in their personal network to play games together.

**Social Networking.** The FunTown platform provides an online social networking community called FunTown Village, in which players meet each other through their online avatars. In FunTown Village, players can interact and communicate, purchase virtual items, and even get married virtually. FunTown plans to introduce more virtual items within FunTown Village to address the strong social interests of its players and to help increase FunTown's overall appeal as a distinct online game community.

**Customer Services.** FunTown provides support and services to its customers primarily through walk-in customer service centers in Taipei and Hong Kong and e-mails and in-game report system where players can inquire and receive responses from FunTown.

**Other Platforms.** FunTown expects to launch its current online games onto other platforms, including Android platform and Apple's iOS platform and to allow data synchronization between each of these platforms.



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### ***Our Marketing***

Our marketing strategy is to capitalize on our established brand names and utilize our diverse distribution networks to retain our existing users and attract new users. We use various qualitative and quantitative market research methods to analyze our target market and to differentiate our product offerings from those of our competitors. We are engaged in a variety of traditional and online marketing programs and promotional activities, including the following:

#### *In-Game Events and Marketing*

We organize in-game events for our users, which we believe encourages the development of online communication and teamwork among our users and increases user interest in our games. Examples of in-game events include scheduled challenges or competitions for prizes. In addition, we use in-game events to introduce new features of our games.

#### *Open Beta Testing*

Our open beta testing is conducted under open market conditions. During open beta testing, we do not charge users to play the new game. Open beta testing serves important marketing functions, including instilling initial interests, establishing an initial user base, and generating word-of-mouth publicity to support the following commercial launch of the game.

#### *Advertisements and Offline Promotions*

We advertise our brand names and our games across a variety of media, including newspapers, the Internet, television and radio, as well as in university campus advertisements and outdoor advertisements. From time to time we distribute game-related posters, promotional prepaid cards for new users and souvenirs at trade shows, selected Internet cafés and other locations. We have contracted with various Internet café unions directly or via agents to promote our games in Internet cafés. We also conduct events at popular venues to stage exhibitions, distribute software and game content-related merchandise, and interact directly with our users.

#### *Magazines*

In addition to advertising certain games in various magazines, we also collaborate with certain entertainment magazines for various promotions, including giving away copies of certain games free of charge with each magazine sold.

#### *New Media Promotion*

In addition to advertising certain games in conventional channels described above, we also collaborate with certain new media channels, for example, with micro-blogging services provided with websites and search engine services.

#### *Direct Marketing*

We use telemarketing and e-mail correspondence to inform our users of new games, promotions and other game-related services.

### ***Our Distribution and Payment Channels***

We sell game points for our online games through various channels. Our distribution and payment channels include:

#### *Offline Physical Distribution Channels*

Physical distribution channels include convenience chain stores, gaming and related retail stores, supermarkets and Internet cafés. At these locations, users may purchase pre-paid game cards with varying amounts of game points. Alternatively, users may purchase game packs to play specific games on FunTown.

#### *Internet-Based Distribution Channels*

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Internet-based distribution channels consist of various websites, including the official website of FunTown. Users may purchase game points through these websites with their credit cards or computer-based payment processing terminals.

### *Telecommunication Network Operators*

We also distribute game points through cooperation with telecommunication network operators and their service providers. Our cooperating operators and service providers charge the fees to the purchasers' phone bills, which are prepared and collected by the network operators.

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### *Payment Aggregators*

We also work with established payment aggregators. These payment aggregators allow users to pay for a variety of products and services, such as mobile phone calls and game points of different game operators, using their pre-paid scratch cards, vouchers or codes printed on receipts.

We sell our game points to distributors at prices lower than the face value of the game points. The costs of distributing game points through Internet-based channels are generally lower than the costs involved in offline distribution of physical game cards. To encourage use of the Internet-based channels and provide more convenience for users, in certain markets we give our users the computer-based payment processing terminals for free so that they can purchase game points online.

### *Our Operation Architecture*

We have a scalable and modular operation architecture that enables us to support and expand our game offerings and services. The architecture consists of several key subsystems, including game services, central user database, billing and payment, online customer service, game telemetry and monitoring. FunTown, has its own unified user account system, which allows players to use a single account to access all FunTown games. Our billing and game management system supports various billing models and deposit options, and is sufficiently flexible to accommodate in-house developed games and licensed games. Our customer service system enables us to assist our players inside and outside the games. Our game telemetry and monitoring system allows us to track our concurrent online users in real time and effectively identify and fix technical problems in our server network.

### *Technology Infrastructure*

Due to the real-time interaction among thousands of users, the stable operation of our online games requires a significant number of servers and a significant amount of connectivity bandwidth. We have developed an extensive technology infrastructure that supports the operation of our online games.

We seek to adapt our infrastructure promptly in response to changing circumstances. This includes operating our games on servers in Macau, Hong Kong, and in the future the PRC.

### *Our Players*

In Taiwan and Hong Kong, as of March 31, 2013, we had an aggregate of about 12 million unique registered players of our online games, more than 70 percent of which were located in Taiwan. In the month of December 2012, we recorded over 288 thousand paying players and approximately 40 thousand peak concurrent users.

### *Competition*

Our primary competitors in the Asian online game and service business are online game operators based in Taiwan and the PRC. Our major competitors in Taiwan include Gamania, Soft-World, IGS, UserJoy and GodGame. Our major competitors in the PRC include Shanda, Giant, Changyou, The9 Limited, Nineyou, Tencent, Perfect World, Kingsoft, Ourgames.com and Chinagames.net.

In addition, we compete for users against various offline games, such as console games, arcade games and handheld games, as well as various other forms of traditional or other online entertainment.

We expect more online games operating companies to enter into the markets where we operate, and a wider range of online games to be introduced to these markets given the relatively low entry barriers to entry in the online games industry. Our competitors vary in size and include private and public companies, many of which have greater financial, marketing and technical resources as well as name recognition. We intend to continue to enhance our market position through providing competitive products and quality services that meet market trends and users preferences, as well as strengthening sales effectiveness.

## **Cloud Computing Business**

### *Overview*

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Our newly launched cloud computing business, GigaCloud, is a provider of cloud computing solutions and related services. The business was founded on the concept of delivering via the Internet, or cloud, integrated tools and services designed to help small-to-medium enterprises ( SMEs ) in Greater China effectively manage complex and dynamic operating environments. We provide our customers highly adaptable, accessible and reliable services and tools to manage critical business functions that enable them to optimize their financial and human capital resources.

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GigaCloud's mission is to simplify and improve the way SMEs acquire, deploy and manage their hardware, software, security and data management technology needs. GigaCloud's offerings enable firms to either avoid deployment of a full-scale onsite IT infrastructure or replace an existing company's internal IT infrastructure with an externally managed and hosted IT function. This virtualization of SMEs can eliminate excess costs and enhance return on investment, promoting the development of boutique businesses that might otherwise find it challenging to compete and grow.

Our initial offerings may be organized into two main product groups:

- a. Communication-oriented services, including hosted private branch exchange (PBX) telephone systems that create private telephone networks within an enterprise, and hosted Internet fax service enabling faxes to be sent via smart devices; and
- b. Value-added services, including hosted video camera surveillance systems that enable users to view video via smart devices, hosted cloud storage, and other related services.

Our products are intuitive and easy to use, can be deployed rapidly, customized easily and integrated with other platforms and enterprise applications. We deliver our solutions as a service via all the major Internet browsers and on most major mobile device operating systems.

### ***Industry Information***

#### ***The Market is Large***

According to a survey completed in 2011 by Taiwan's Ministry of Economic Affairs, Taiwan's SME market size was estimated at approximately 1.24 million enterprises.

#### ***Changes in the Business Environment, User Expectations, and Technology are Driving Change***

We believe that the convergence of cloud, social, and mobile technologies is transforming how companies connect with their customers, employees, partners and products; as businesses look to operate their IT systems in a more cloud-like manner, they will seek to spend less time and effort on developing underlying infrastructure and focus more on re-imagining, re-platforming, and virtualizing their businesses. Our strategy of cloud infrastructure, application platform capabilities for new and renewed applications, and client management capabilities for the post-PC era will provide customers an extended suite of software to address the integration, automation, management, and development capabilities they need.

### ***Strategic Partnerships***

To address the market opportunity, we have formed strategic partnerships with a broad group of hardware, software and cloud computing service vendors to cooperatively advance virtualization technology for SMEs through joint marketing, product interoperability, collaboration and co-development. These partners include Taiwan's telecom leader Far EasTone, global computer hardware and electronics leader Asus, and leading PDF document solutions provider Foxit Corporation. We create opportunity for partners by enabling them to build products that utilize our SME virtualization technology and create differentiated value through joint solutions. The endorsement and support of our partners further enhances the awareness, reputation and adoption of our virtualization solutions.

We have also developed a multi-channel distribution model to expand our presence and reach various segments of the market. Our distribution partners include Atos SE and Chailease Holding Co Ltd. Based in France, Atos is an international IT services and consulting company. Atos provides consulting and technology services, as well as managed services and systems, to a global client base. Taiwan-based Chailease Holding Co Ltd. is Taiwan's number one leasing company with approximately 42 percent market share in the business leasing market. The firm has a wide product offering, including financial services, leasing, and installment sales and serves approximately 15,000 SMEs in Greater China. Management believes GigaCloud will benefit from the distribution capabilities and large customer bases of these partners.

### ***Intellectual Property***

We rely on a combination of patent, trademark, copyright and trade secret laws in the U.S. and Taiwan as well as confidentiality procedures and contractual provisions to protect our proprietary technology and our brand. We have patents, copyrights and trademarks in certain jurisdictions

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and may apply for further trademark and copyright registrations and additional patents, which may provide such protection in relevant jurisdictions. However, there is no assurance that this will be sufficient to fully protect our proprietary technology. In addition, our technologies may not be able to withstand any third-party claims or rights against their use.

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We also enter into confidentiality and invention assignment agreements with our employees and consultants and confidentiality agreements with other third parties, and we rigorously control access to proprietary technology.

### **Regulation**

#### ***Regulations Relating to Online Games in Taiwan***

At present, there is no specific law in Taiwan governing online game services, nor are there any specific licensing requirements imposed on Internet content providers in connection with offering online game services. The National Communications Commission (the NCC) was established in March 2006. In December 2006, the NCC proposed the overhaul of the regulatory framework in the communications and broadcasting sectors by amending the Telecommunications Act, the Radio and Television Act, the Cable Radio and Television Act and the Satellite Radio and Television Act. Pursuant to the original proposal, the legislation at issue would be consolidated into a new legislative Act to be known as the Communications and Broadcasting Act. In December 2008, the NCC announced a change to its policy, stating that it had decided to delay enacting the Communication and Broadcasting Act for two to four years. According to the digital convergence plan adopted by the Executive Yuan in December 2010, digital convergence framework is expected to be approved in 2014 and digital convergence law is expected to be finalized in 2015.

#### ***Rating of Internet Content***

The Government Information Office, which was the agency in charge of Internet content prior to establishment of the NCC, promulgated the Regulations for the Rating of Internet Content in April 2004, as amended in October 2005. In general, Internet content shall not include any illegal or banned materials. To avoid negative impact on the physical or mental development of children or adolescents, Internet content containing any of the following materials shall be rated as restricted and shall not be viewed by those below the age of 18: (i) excessive depiction of gambling, robbery or other criminal offenses; (ii) excessive depiction of suicide; (iii) depiction involving terror, blood or cruelty which is presented in a manner acceptable to adults; or (iv) depiction of sexual acts or sexual obscenity which does not embarrass or disgust adults in general. If Internet content is in violation of the Regulations for the Rating of Internet Content, competent authorities may order the relevant ISPs to restrict access to children or adolescents or remove the offending content and impose an administrative fine on the offenders.

#### ***Computer Software Ratings***

The Ministry of Economic Affairs announced in July 2006 the Regulations Governing Computer Software Rating, which took effect in January 2007. This regulation was first amended in June 2009 and the first amendment took effect in December 2009 and further amended on March 10, 2011 and took effect on July 1, 2011. Computer software includes the game software which can be installed in computers, televisions and handheld gaming devices. The provider of computer software shall identify the rating of the computer software when it provides it to users. There are four ratings: (i) Mature Audience Only (not suitable for those below the age of 18); (ii) Parental Guidance Advisable (not suitable for those below the age of 12; parental guidance is advisable for those between the ages of 12 to 18); (iii) Parental Guidance Strongly Suggested (not suitable for those below the age of 6; guidance from parents, teachers or adults is strongly suggested for those between the ages of 6 to 12); and (iv) General Audience (suitable for all ages). According to the 2011 amendment, the computer gaming software that uses virtual currency to play simulated MahJong, poker, dice, steel ball, horse racing, roulette, slot machine and other games of similar nature, and the outcome of the games may result in increase or decrease of the virtual currency, shall be rated as Parental Guidance Strongly Suggested. If the contents thereof meet the requirements under the rating criteria of Mature Audience Only or Parental Guidance Advisable, such games shall be rated accordingly.

#### ***Online Game Contract Template***

The Ministry of Economic Affairs and the Consumer Protection Commission have published a model contract template which sets out permitted terms and limitations with respect to online game services offered in Taiwan, pursuant to the Consumer Protection Act. The contract template was last amended on December 7, 2010. Generally, consumers should be given at least three days to review such contract. Amendments or changes to fees payable for services offered must be publicly announced at least thirty days prior to such amendment, and notification provided to consumers. Consumer game records must be maintained by each online game operator for a minimum period of thirty days and shall be open to inspection by such consumers. Suspension periods for consumers who have breached the terms of their online game contracts may not exceed a period of seven days. Apart from gifts, the on-line game operator cannot limit the use period of the game points in the on-line game contract. Furthermore, the on-line game operator cannot specify in the on-line game contract that it has the right to interpret the contract terms and conditions.





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*Personal Data Protection Act*

On April 27, 2010, the Legislative Yuan passed a bill to amend the Computer-processed Personal Data Protection Act, which was renamed as the Personal Data Protection Act. Whenever an entity collects personal data from any individual, it shall inform such individual about (i) the name and identity of the collecting entity; (ii) the purpose of collection; (iii) how the collected personal data will be used; (iv) his/her rights; and (v) the consequences of his/her failure to provide the required personal data. If personal data is not provided by individuals, in addition to the information required to be disclosed as described above, the collecting entity shall inform such individual of the source of the data before processing or using the data. In principle, prior consent from the individual is required for use of his/her personal data. These requirements shall be exempted if relevant personal data of the individual (i) is used for public interests; or (ii) is available from the public domain and the interest to be protected is more important than the privacy of such individual. Depending on the gravity of a violation, damages of NT\$500 to NT\$20,000 may be claimed against a person for each violation of the Personal Data Protection Act even if the actual damage cannot be proved. If there is more than one victim in a single violation, the maximum damages would be up to NT\$200,000,000. However, if the interests involved therein exceed NT\$200,000,000, restrictions on maximum amount for damages to be claimed and on minimum amount for damages to be claimed (NT\$500 per person for each violation) shall not apply. This new Personal Data Protection Act will take effect pursuant to the announcement of the Executive Yuan. Given that there may be some delay in the enactment of the enforcement rules, the new Personal Data Protection Act will come into force sometime in 2012.

*Regulations Relating to Online Games in Singapore*

Presently, there are no laws in Singapore which specifically govern the provision of online gaming. However, depending on the type of games offered and services rendered as part of our online gaming operations, the operations may be subject to regulation under various Singapore legislation. Relevant legislation includes:

the Broadcasting Act (Chapter 28) of Singapore (the Broadcasting Act ) and its subsidiary legislation, which regulates, inter alia, the operation of Internet websites;

the Telecommunications Act (Chapter 323) of Singapore (the Telecommunications Act ) and its subsidiary legislation, which regulates the operation of telecommunications systems and the provision of telecommunications services; and

the Common Gaming Houses Act (Chapter 49) of Singapore (the CGH Act ) and the Betting Act (Chapter 21) of Singapore (the Betting Act ) and subsidiary legislation, which regulate, inter alia, gaming and lotteries.

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### *Broadcasting Act*

The Broadcasting Act provides for the general legal framework to regulate media and Internet content and empowers the Media Development Authority ( MDA ) of Singapore with the authority to grant licenses and to regulate and monitor licensees in relation to such media and Internet content. In particular, section 8 of the Broadcasting Act provides that no person shall provide any licensable broadcasting service in or from Singapore without a broadcasting license granted by the Authority (MDA) . A licensable broadcasting service is defined in the Broadcasting Act to include computer on-line services .

The MDA also regulates online services through the Broadcasting (Class License) Notification (the BCLN ). Under the BCLN, VAN computer on-line services (as defined in the BCLN) and computer on-line services that are provided by Internet Content Providers and Internet Service Providers (as such terms are defined in the BCLN) are deemed automatically licensed, and the licensees under the class license must comply with the conditions of the class license under the BCLN. The definition of Internet Content Provider under the BCLN includes any corporation or group of individuals, whether registrable or incorporated under the laws of Singapore, who provides any programme on the World Wide Web through the Internet. A programme is defined under the Broadcasting Act to mean, broadly, any matter the primary purpose of which is to entertain, educate or inform all or part of the public, or any advertising whether commercial or not, excluding any matter that is wholly related to or connected with any private communication.

Pursuant to the BCLN, a licensee must use its best efforts to ensure that its service complies with the codes of practice which may be issued by the MDA from time to time (including the Internet Code of Practice), and is not used for any purpose and does not contain any programme that is against the public interest, public order, national harmony or offends against good taste or decency. Further, licensees must also ensure that its services are not used for, or in furtherance of, certain prohibited activities such as games and lotteries the conduct of which is an offence under the CGH Act, the advertisement or promotion of astrology, geomancy, palmistry or any other type of fortune telling device or the solicitation of prostitution or any other immoral activity.

Under the Internet Code of Practice issued by the MDA, an Internet Content Provider is required to ensure that it does not broadcast via the Internet to users in Singapore, programs which include material that is objectionable on the grounds of public interest, public morality, public order, public security, national harmony or is otherwise prohibited by applicable Singapore laws ( prohibited materials ). The Internet Content Provider is also required to deny access to such prohibited materials that he discovers in the normal course of exercising editorial duties, or is informed about.

### *Telecommunications Act*

The provision and operation of telecommunication services and systems in Singapore is regulated by the Telecommunications Act, which provides the general legal framework for the provision and operation of telecommunication systems and services in Singapore.

Under the Telecommunications Act, all persons who, inter alia, establish, install, maintain, develop or hire a telecommunication system or service within Singapore must be licensed by the Info-communications Development Authority ( IDA ) of Singapore. A telecommunication system is defined as any system used or intended to be used for telecommunications, and telecommunication service is defined as any service for telecommunications but excludes any broadcasting service. Telecommunications is defined as a transmission, emission or reception of signs, signals, writing, images, sounds or intelligence of any nature by wire, radio, optical or other electro-magnetic systems whether or not such signs, signals, writing, images, sounds or intelligence have been subject to rearrangement, computation or other processes by any means in the course of their transmission, emission or reception.

The existing telecommunications licensing framework provides for two broad categories of licenses facilities based operator ( FBO ) licenses and services based operator ( SBO ) licenses. SBO licenses are, in turn, granted either on an individual or class license basis.

Pursuant to IDA s published guidelines, the telecommunications services which are provided as licensable under an SBO license include store-and-retrieve value-added network services, examples of which include any online information and database retrieval services, online games or electronic chatting services, provided by telecommunication systems, built over and above the telecommunication systems operated by an FBO and accessed through public telecommunication systems or leased circuits, which allow telecommunication traffic between a user and the value-added network or between users.

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### *CGH Act and Betting Act*

Depending on the type of games and services being offered, the online gaming operations may also be regulated by the CGH Act and the Betting Act. Generally, the CGH Act and the Betting Act prohibit the operation and patronization of unlicensed common gaming and betting houses as well as ancillary acts. In addition, the CGH Act prohibits the operation of and participation in a public lottery. The offences are wide-ranging in nature and encompass acts by the owner of the website, the player and assisting parties.

The CGH Act generally prohibits the engaging in gaming activities and arguably applies to gaming activities carried out online. In particular, the CGH Act prohibits, among other things, the following: (i) gaming in a common gaming house (as such term is defined in the CGH Act) or a public place; (ii) participation or assistance in any public lottery; (iii) advancing or furnishing money for the purpose of establishing or conducting the business of a common gaming house; and (iv) assisting in any manner in the management of a place kept or used as a common gaming house. Under the CGH Act, gaming is defined as the playing of any game of chance or of mixed chance and skill for money or money's worth. Lottery includes any game, method, device, scheme or competition whereby money or money's worth is distributed or allotted in any manner depending upon or to be determined by chance or lot, whether the same is held, drawn, exercised or managed within or without Singapore. A public lottery is defined as a lottery to which the public or any class of the public has or may have access, and every lottery shall, until the contrary is proved, be deemed to be a public lottery.

The Betting Act generally prohibits betting or wagering on any event or contingency of or relating to any horse-race or any other race, fight, game, sport or exercise, and would arguably also apply where such betting or wagering is conducted online. In particular, the Betting Act prohibits, inter alia, the following: (i) betting or wagering in a common betting-house or with a bookmaker (as such terms are defined in the Betting Act) in any place or by any means; (ii) the receipt (directly or indirectly) of any money or valuable thing for or in respect of any bet or wager on any such event or contingency in a common betting-house or betting information centre (as defined in the Betting Act); (iii) the advancing or furnishing of money for the purpose of establishing or conducting the business of a common betting-house; and (iv) assisting in any manner in the management or in the business of a place kept or used as a common betting-house or betting information centre.

### **Dividends from Our Subsidiaries**

Under Singapore tax regulations, foreign-sourced dividend income used for capital expenditures, including investments, and repayment of borrowings, is not deemed as remitted to Singapore and is therefore not taxable.

### **Listing and Offering**

Under NASDAQ Rule 5210(c), as amended ( Rule 5210(c) ), all securities listed on NASDAQ must be eligible for a direct registration program, or DRS, operated by a registered clearing agency, unless the foreign private issuer is prohibited from complying by a law or regulation in its home country. In order to fulfill the direct registration program eligibility requirements, we are required to, among other provisions, amend our constitutional documents to allow for the issue of non-certificated securities.

Our Company is incorporated under the laws of the Republic of Singapore and is subject to the provisions of the Companies Act (Cap.50) of Singapore (the Companies Act ). Under the Companies Act, Singapore-incorporated companies are required to issue physical share certificates to registered shareholders as prima facie evidence of a registered shareholder's title to the Shares and there are no exceptions to or exemptions from this requirement that would enable us to amend our constitutional documents to allow for the issue of non-certificated shares. Therefore, we are not able to comply with the DRS eligibility provisions of Rule 5210(c).

Under the DRS eligibility provisions, as a foreign private issuer, we are allowed to follow our home country practice in lieu of the requirements set out in Rule 5210(c), subject to certain exceptions. We will be relying on this for an exemption from the DRS eligibility requirements under Rule 5210(c). We have informed the NASDAQ Stock Market about our election to comply with the laws of Singapore in lieu of the DRS eligibility provisions of Rule 5210(c).

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**C. Organizational Structure**

We were incorporated in Singapore as a company limited by shares on September 13, 1999. As of the date of this annual report, our principal operating subsidiaries include Hoshin GigaMedia, FunTown World Limited, and GigaMedia Cloud. Hoshin GigaMedia, our wholly owned subsidiary incorporated in Taiwan, operates our Asian online game and service business in Taiwan. FunTown World Limited, our wholly owned subsidiary incorporated in the British Virgin Islands, operates our Asian online game and service business in Hong Kong and Macau. GigaMedia Cloud, our wholly owned subsidiary incorporated in Taiwan, operates our GigaCloud services in Taiwan.

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The following organization chart and table set forth our business structure and selected information for each of our principal subsidiaries as of the date of this annual report:

Includes our operating subsidiaries or companies holding material investments or contracts only. All subsidiaries are 100% owned unless otherwise indicated.

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| <b>Entity</b>   | <b>Year of Incorporation</b> | <b>Place of Incorporation</b> | <b>Our Percentage Holding</b> | <b>Principal Activities</b>                   |
|---|------------------------------|-------------------------------|-------------------------------|---|
| <b>Held by our Company</b>                              |                              |                               |                               |   |
| GigaMedia International Holdings Limited                | 2004                         | British Virgin Islands        | 100%                          | Holding company                               |
| <b>Held by GigaMedia International Holdings Limited</b> |                              |                               |                               |   |
| GigaMedia Online Entertainment Corp.                    | 2009                         | Cayman Islands                | 100%                          | Holding company                               |
| Cambridge Entertainment Software Limited                | 2004                         | British Virgin Islands        | 100%                          | Holding company                               |
| GigaMedia (HK) Limited                                  | 2004                         | Hong Kong                     | 100%                          | Holding company                               |
| <b>Held by GigaMedia Online Entertainment Corp.</b>     |                              |                               |                               |   |
| FunTown World Limited                                   | 2005                         | British Virgin Islands        | 100%                          | Holding company                               |
| GigaMedia Asia Pacific Limited                          | 2005                         | British Virgin Islands        | 100%                          | Holding company                               |
| GigaMedia Capital Limited                               | 2007                         | British Virgin Islands        | 100%                          | Holding company                               |
| Dragon Mark Holdings Limited                            | 2009                         | British Virgin Islands        | 100%                          | Holding company                               |
| Premier Vantage Holdings Limited                        | 2009                         | British Virgin Islands        | 100%                          | Holding company                               |
| GigaMedia Freestyle Holdings Limited                    | 2009                         | British Virgin Islands        | 100%                          | Holding company                               |
| GigaMedia (Labuan) Limited                              | 2005                         | Labuan                        | 100%                          | Holding company                               |
| Megabiz Limited   | 2010                         | British Virgin Islands        | 100%                          | Holding company                               |
| <b>Held by Dragon Mark Holdings Limited</b>             |                              |                               |                               |   |
| Wolverine Holdings Group Limited                        | 2009                         | British Virgin Islands        | 100%                          | Holding company                               |
| <b>Held by FunTown World Limited</b>                    |                              |                               |                               |   |
| FunTown Hong Kong Limited                               | 1999                         | Hong Kong                     | 100%                          | Dormant                                       |
| <b>Held by GigaMedia (Labuan) Limited</b>               |                              |                               |                               |   |
| Leisure Alliance Sdn. Bhd.                              | 2009                         | Malaysia                      | 100%                          | Holding company                               |
| <b>Held by Leisure Alliance Sdn. Bhd.</b>               |                              |                               |                               |   |
| Hoshin GigaMedia Center Inc.                            | 1998                         | Taiwan                        | 100%                          | Online games                                  |
| GigaMedia Cloud Services Co., Ltd.                      | 2011                         | Taiwan                        | 100%                          | Cloud Computing Services                      |
| <b>Held by GigaMedia (HK) Limited</b>                   |                              |                               |                               |   |
| GigaMedia Europe Limited S.à.r.l.                       | 2010                         | Luxembourg                    | 100%                          | Dormant                                       |
| <b>Held by Cambridge Entertainment Software Limited</b> |                              |                               |                               |   |
| Cambridge Interactive Development Corporation           | 1997                         | U.S.A.                        | 100%                          | Software development and application services |
| Internet Media Licensing Limited                        | 2005                         | British Virgin Islands        | 100%                          | Software development and application services |

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**D. Property, Plant and Equipment**

As of March 31, 2013, we leased approximately 47,137 square feet as office premises as our corporate head office in Taipei, Taiwan and approximately 4,831 square feet as office premises for FunTown's office in Hong Kong. In addition, we leased approximately 1,265 square feet of warehouse space in Hong Kong.

**ITEM 4A. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

Unless stated otherwise, the discussion and analysis of our financial condition and results of operations in this section apply to our consolidated financial statements as prepared in accordance with U.S. GAAP. You should read the following discussion of our financial condition and results of operations together with the consolidated financial statements and the notes to these statements included elsewhere in this annual report.

**A. Operating Results**

**Overview**

We are a holding company. Through July 2012, we operated two principal businesses through our subsidiaries and equity method investees:

Our Asian online game and service business operates a portfolio of online games, primarily targeting online game players across Asia, including Greater China and Southeast Asia.

Gaming software and service business, of which we held a controlling equity interest through July 2012, develops and licenses online poker, casino, and sports betting gaming software solutions and application services, primarily targeting continental European markets.

We continue to operate our Asian online game and service business and we began developing a new cloud computing business in the second half of 2012. The cloud business aims at providing an integrated platform of services and tools for small-to-medium enterprises in Greater China to increase flexibility, efficiency and competitiveness. The business launched in early April 2013.

In 2012, we recorded total operating revenues of approximately US\$27.5 million, a decrease of approximately US\$6.9 million year-over-year, primarily from a decrease of approximately US\$4.2 million resulting from our sale of a 60 percent interest and subsequent deconsolidation in IAHGames in August 2012. Our total costs and expenses decreased by approximately US\$6.3 million year-over-year to US\$48.0 million. We recorded an operating loss of approximately US\$20.6 million, an increase of approximately US\$645 thousand year-over-year. We recognized a net loss attributable to us of approximately US\$15.3 million, a loss reduction of approximately US\$55.9 million year-over-over, primarily resulting from net losses in 2011 of approximately US\$61.2 million on equity method, marketable securities and cost method investments, compared to net losses of approximately US\$1.0 million in 2012.

*Asian Online Game and Service Business.* We operate our Asian online game and service business in Taiwan, Hong Kong and Macau through FunTown. We acquired FunTown in January 2006 and consolidated the financial results of FunTown into our consolidated financial statements starting from January 1, 2006. Previously, we operated in the PRC through a variable interest entity, JIDI, until our board of directors approved a plan to liquidate and dissolve JIDI in June 2012. In Southeast Asia, we operated through IAHGames. We increased our ownership percentage in IAHGames from 32.26 percent in 2006 to 80 percent in 2010 through the acquisition of certain preferred shares and the subscription for new preferred shares and consolidated IAHGames' financial results into our consolidated financial statements starting from July 1, 2010. In July 2012, we entered an agreement to sell a 60 percent ownership in IAHGames, and, upon the closing of the agreement, we deconsolidated the results of IAHGames' operations and began accounting for our remaining 20 percent interest under the equity method. The complete divestiture of IAHGames was agreed in April 2013 and is expected to conclude on May 2, 2013.

In addition to our majority-controlled subsidiaries, we also entered into strategic alliances with SoftStar, XL Games, Access China, Gorilla Banana Entertainment, JC Entertainment Corporation, Possibility Space Incorporated, and East Gate in June 2007, December 2007, January

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2008, May 2009, September 2009, December 2009, and August 2010, respectively. SoftStar is an online game development and publishing company incorporated in Taiwan. XL Games was founded by the creator of one of the most popular online game franchises in history and focuses on MMORPGs with studios in Seoul, South Korea and Austin, Texas. Access China is an online game software developer in the PRC. Gorilla Banana Entertainment is an online game software developer in Korea. JC Entertainment Corporation is a publicly-listed company which develops online games in Korea. Possibility Space Incorporated is an online game software developer in the PRC. East Gate is a Korean fund which invests in online game businesses and films.



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Online casual game operators in Greater China and Southeast Asia are currently our primary competitors. We also compete with MMORPG operators throughout Greater China and Southeast Asia. Given the low barriers to entry in the online game industry and the increasing popularity of Internet-based businesses, there are a large number of potential competitors scattered throughout many different segments of the software and Internet industries. In addition to the aforementioned competitors, traditional entertainment service providers and other entities, many of which have significant financial resources and name brand recognition, may provide online game services in the future, and thus become our competitors.

Faced with our known competitors, and most likely several new competitors which may be established in the near future, we will continue to improve the principal competitive factors that we believe can differentiate our product offerings from those offered by our competitors, including: brand, technology, financial stability and resources, proven track record, independent oversight and transparency of business practices in our industry.

In 2012, our Asian online game and service business generated revenue of approximately US\$27.5 million, gross profit of approximately US\$16.1 million, operating loss of approximately US\$ 12.3 million, non-operating income of approximately US\$4.9 million, and net loss attributable to us of approximately US\$9.8 million.

*Gaming Software and Service Business.* Until April 8, 2010, we operated our gaming software and service business through our subsidiary, Cambridge Entertainment Software Limited ( CESL ), and through its wholly-owned subsidiaries, Cambridge Interactive Development Corporation and Internet Media Licensing Limited. Under the terms of the licenses granted by us to Ultra Internet Media S.A. ( UIM ), we were entitled to a share of the revenues of such licensee, and as such, we had certain economic risks with respect to, and derived certain economic benefits from, their operations. Therefore, through March 31, 2010, the financial results of UIM were incorporated into our consolidated financial statements as UIM met the criteria of a VIE as defined by the FASB Accounting Standards Codification.

On April 8, 2010, we sold a 60 percent interest in our gaming software and service business to Mangas Gaming S.A.S., a French Corporation, now renamed as BetClic Everest Group ( BetClic ), and deconsolidated the gaming software and service business as we ceased to have a controlling financial interest from that date. Our remaining ownership interest in the gaming software and service business was accounted for under the equity method starting from April 2010 to August 2012 when we entered in to an agreement with BetClic to sell our remaining ownership interest. See note 6 to our consolidated financial statements for additional information.

The holding and disposal of our remaining non-controlling interest in the gaming software and service business generated net gain of approximately US\$2.5 million for the year ended December 31, 2012, which was directly related to the sale of our remaining ownership interest in such business in July 2012.

### **Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012**

#### ***Divestiture of Gaming Software and Service Business***

On December 15, 2009, we entered into an agreement with BetClic to sell 60 percent of substantially all of the assets and liabilities of our gaming software and service business for approximately US\$100 million in cash, subject to certain adjustments. The closing of the sale occurred on April 8, 2010. The sale resulted in the recognition of a gain of US\$79.1 million, net of transaction costs. The sale of the remaining 40 percent was subject to a put and call mechanism in place between us and BetClic, as defined in the agreement. We had the option to put all or part of our remaining 40 percent ownership interest to BetClic in each of 2013, 2014, and 2015 at a value considering all relevant facts and circumstances after the end of each year. If the put option owned by us was not fully exercised, BetClic would have the option to call the remaining interest held by us in each of 2015 and 2016.

We deconsolidated the gaming software and service business and recognized a gain when we completed the sale of 60 percent of substantially all of the assets and liabilities to BetClic on April 8, 2010, which was the date that we ceased to have a controlling financial interest. The remaining ownership interest we retained in the gaming software and service business, a 40 percent interest later diluted to 33.66 percent, was accounted for under the equity method starting from April 2010 to July 2012, when we entered into another agreement with BetClic to sell our remaining ownership interest in the gaming software and service business for a consideration of US\$1.7 million. Of this consideration, US\$985 thousand was paid to us in cash, while the remainder related to the extinguishment of a 2009 tax liability. The closing of the sale occurred in August 2012. The sale resulted in the recognition of a gain of US\$2.5 million, net of transaction costs. In 2010, 2011 and 2012, we recorded equity investment losses relating to our remaining non-controlling interest of US\$9.8 million, US\$49.7 million and US\$0, respectively.



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Our Company accounted for the deconsolidation of the gaming software and service business at fair value and recognized a gain of US\$79.1 million in 2010 measured as the difference between:

|   | <b>Amount<br/>(in US\$<br/>thousands)</b> |
|---|---|
| The fair value of any consideration received, including purchase price adjustments, net of any transaction costs                                      | \$ 82,984                                 |
| The fair value of the 40% retained non-controlling investment in the gaming software and service business at the date the business was deconsolidated | 54,240                                    |
| Less: The carrying amount of the gaming software and service business at the date of the deconsolidation  | (58,084)                                  |
| <br>Gain on deconsolidation of the gaming software and service business   | <br>\$ 79,140                             |

***Acquisition and Divestiture of IAHHGames***

In July 2010, we began consolidating IAHHGames, an online game operator, publisher and distributor in Southeast Asia. We acquired IAHHGames in order to enhance our position in the online game market in Southeast Asia and strengthen our online entertainment product portfolio. This primary factor among others, contributed to a purchase price in excess of the fair market value of the net tangible assets and intangible assets acquired.

As of December 31, 2010 and 2011, we owned 5,982,230 Class A preferred shares and 1,208,881 Class B preferred shares of IAHHGames, which represents a controlling financial interest of 80 percent of the total outstanding voting rights of IAHHGames. The preferred shares (Class A) were convertible into ordinary shares of IAHHGames at a conversion rate of 10 Class A shares for 1 ordinary share. The preferred shares (Class B) were convertible into ordinary shares of IAHHGames at a conversion rate of 1 Class B share for 1 ordinary share.

In July 2012, we entered into agreements to sell 100 percent of the shares of Spring Asia, an investment holding company which owns 30 percent of the shares of Game First International Corporation ( GFI ), to IAHHGames, as well as a 60 percent ownership in IAHHGames (with a 20 percent ownership of IAHHGames retained by us) to IAHHGames management and Management Capital International Limited, a British Virgin Islands company owned by IAHHGames management.

In consideration for sale of IAHHGames and Spring Asia, we are to receive US\$3 million in cash consideration in four equal installments, with the first due upon closing, the second due on October 2, 2012, the third due on January 2, 2013 and the fourth due on April 2, 2013. The first installment of US\$750 thousand was received upon the closing on August 15, 2012. However, the second, third, and fourth installments remain outstanding. The payments are collateralized by the shares of Spring Asia, which are only released from the escrow in proportion to the payment made upon each installment.

In April 2013, we entered into the IAH Settlement Agreement to settle the outstanding Spring Asia purchase price of US\$2.25 million. Under the IAH Settlement Agreement, we also sold all of our remaining shares in IAHHGames to MCIL (approximately 20% of IAHHGames total issued and outstanding shares) at a purchase price of US\$1 million. For further information, see Item 3 Key Information D. Risk Factors.

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Our Company accounted for the deconsolidation of and the retained noncontrolling investment in IAHGames in August 2012 at fair value. Considering the uncertainty as to the collectability of the remaining three installments, we deferred the disposal gain of US\$211 thousand against the consideration installments receivable of US\$2.25 million as of December 31, 2012. The deferred gain is measured as the difference between:

| (In US\$ thousand)  | Amount   |
|---|----------|
| The fair value of consideration received and receivable, net of any transaction costs, plus           | \$ 3,000 |
| The fair value of the 20% retained noncontrolling investment in IAH at the date of deconsolidation    |          |
|   | 3,000    |
| The carrying amount (credit balance) of IAHGames at the date of deconsolidation                       | (14,536) |
| Net receivables due to GigaMedia from IAHGames waived upon the closing of the sale                    | 17,542   |
| Other comprehensive income component of equity related to IAHGames at the date of the deconsolidation | (217)    |
|   | 2,789    |
| Deferred gain on deconsolidation of IAH   | \$ 211   |

**Consolidation of Monsoon**

We, through IAHGames, made an equity investment in Monsoon, an operator and distributor of online games in Southeast Asia, in connection with our acquisition of a controlling financial interest in IAHGames with effect from July 1, 2010. In connection with a strategic alliance, Monsoon entered into various agreements with Blizzard Entertainment International, a division of Coöperatie Activision Blizzard International U.A. ( Blizzard ) to distribute selected Blizzard Entertainment games in Southeast Asia (collectively referred to as the Distribution Partnership ). Although IAHGames owns 100 percent of the common stock of Monsoon, Monsoon was not consolidated at the time of the acquisition as Blizzard had substantive participating rights in Monsoon's business operations pursuant to Monsoon's management agreement. In September 2011, IAHGames, Monsoon and Blizzard entered into an agreement whereby they agreed to the early termination of the Monsoon management agreement and other related agreements which granted Blizzard the abovementioned substantive participating rights. The termination agreement was effective from August 31, 2011. Starting from September 1, 2011, IAHGames had effective control over Monsoon and therefore we consolidated Monsoon from that date through the date we deconsolidated IAHGames.

The agreement was effective from the third quarter of 2011. In January 2012, IAHGames and Monsoon's commitments under the Distribution Partnership with Blizzard were fully terminated. The execution and closing of this agreement resulted in the following main financial statement impacts in our consolidated financial statements in 2011:

|   | (in US\$ thousands) |
|---|---------------------|
| Gain on cancellation of warrant liabilities             | \$ 665              |
| Gain on reversal of impairment of prepaid expenses      | 1,347               |
| Recovery of loss on termination of third-party contract | \$ 2,012            |

**Divestitures of JIDI and Shanghai JIDI**

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In June 2012, our board of directors approved a plan to liquidate and dissolve JIDI, a wholly-owned subsidiary, and Shanghai JIDI. Results for JIDI and Shanghai JIDI operations are reported as discontinued operations for all periods presented. The carrying amounts of the remaining assets and liabilities of JIDI and Shanghai JIDI were not significant to our consolidated financial statements as of December 31, 2012, and we recorded a loss of approximately US\$588 thousand in connection with the disposal of property, plant and equipment, which is included within discontinued operations. Summarized selected financial information for discontinued operations of JIDI and Shanghai JIDI are as follows:

| (in US\$ thousands)                          | 2011       | 2012       |
|--|------------|------------|
| Revenue                                      | \$ 29      | \$ 100     |
| Loss from discontinued operations before tax | \$ (4,240) | \$ (2,521) |
| Income tax expense                           |            |            |
| Loss from discontinued operations            | \$ (4,240) | \$ (2,521) |

**Table of Contents****Deconsolidation of T2CN**

In June 2007, we began consolidating T2CN Holing Limited ( T2CN ), an operator and provider of online sports games in the PRC. As of December 31, 2010 and December 13, 2011, we owned 43,633,681 common shares of T2CN, which represented an ownership interest of 67.09 percent of the total outstanding voting rights of T2CN. We disposed of all of our ownership interest in T2CN in December 2011 through a sale to a third party.

As a result of a dispute with T2CN s former Chief Executive Officer, arising in July 2010, we had been prevented from obtaining access to the assets and financial information necessary to report the financial results of T2CN. Therefore, we had effectively lost control over a majority of T2CN s assets and its financial reporting process of that time. In spite of owning 67.09 percent of T2CN s common stock, we deconsolidated T2CN s results with effect from July 1, 2010. The following is a breakdown of our retained investment at the date of deconsolidation.

|                                     | <b>Amount<br/>(in US\$<br/>thousands)</b> |
|-------------------------------------|---|
| Cash                                | \$ 12,903                                 |
| Other current assets                | 1,266                                     |
| Fixed assets/ non-current assets    | 1,679                                     |
| Prepaid licensing and royalty       | 5,339                                     |
| Intangible assets                   | 1,098                                     |
| <br>                                |   |
| Total assets of T2CN                | 22,285                                    |
| Total liabilities of T2CN           | (12,331)                                  |
| <br>                                |   |
| Net equity of T2CN                  | 9,954                                     |
| Noncontrolling interest             | (3,276)                                   |
| Goodwill acquired                   | 17,500                                    |
| Advances to T2CN Operating Entities | 1,405                                     |
|                                     | <br>                                      |
|                                     | \$ 25,583                                 |

In connection with our year-end financial reporting process, we were required to perform an impairment analysis for our Company s investment in and advances to the T2CN Operating Entities as of December 31, 2010. Given we had been prevented from obtaining the financial information necessary to report the financial results of T2CN, and we had effectively lost control over a majority of T2CN s assets and its financial reporting process, we decided to completely write-off both our Company s investment in and its advances to the T2CN Operating Entities in order to properly reflect our financial position as of December 31, 2010. The impairment charges recorded for the investment and the advances in 2010 were approximately US\$22.2 million (after removing the other comprehensive income component of equity related to T2CN from our Company s balance sheet) and approximately US\$1.4 million, respectively.

On December 2, 2011, we entered into an agreement with Hornfull Limited, and Hangzhou NewMargin Ventures Co. Ltd. ( Hangzhou NewMargin ) whereby we agreed to sell all of our ownership interest in T2CN to Hornfull Limited and Hangzhou NewMargin agreed to guarantee the payment and performance of Hornfull Limited under the agreement. On December 14, 2011, the parties completed the sale and purchase of the T2CN shares. Pursuant to the agreement, we sold all of our ownership interest in T2CN to Hornfull Limited in exchange for a cash payment of US\$4.7 million, resulting in a gain of US\$4.7 million being recorded in 2011. Hornfull Limited also reimbursed us US\$0.8 million in cash for legal fees incurred by us in connection with the T2CN dispute.

**Table of Contents****Treatment of T2 Entertainment, T2 Advertisement, and Jinyou before Deconsolidation**

Pursuant to various agreements entered into among T2 Entertainment, T2 Technology and the equity interest owners of T2 Entertainment, until June 30, 2010, T2CN, through its wholly owned subsidiary T2 Technology, had effective control over T2 Entertainment and was considered the primary beneficiary of T2 Entertainment. T2 Entertainment was established to hold the necessary licenses required for the operation of our Asian online game and services business in the PRC. Accordingly, from the date that we consolidated T2CN through July 1, 2010, the date we deconsolidated T2CN (see note 5 to our consolidated financial statements for additional information), the financial results of T2 Entertainment were included in the accompanying consolidated financial statements.

Pursuant to various agreements entered into among T2 Advertisement, T2 Technology and the equity interest owners of T2 Advertisement, until June 30, 2010, T2CN, through its wholly owned subsidiary T2 Technology, had effective control over T2 Advertisement and was considered the primary beneficiary of T2 Advertisement. T2 Advertisement was established to hold the necessary licenses required for the operation of our Asian online game related advertisement services in the PRC. Accordingly, from the date that we consolidated T2CN through July 1, 2010, the date we deconsolidated T2CN (see note 5 to our consolidated financial statements for additional information), the financial results of T2 Advertisement were included in the accompanying consolidated financial statements.

T2 Technology also entered into various agreements with Jinyou and the equity interest owners of Jinyou. Until June 30, 2010, T2CN, through its wholly owned subsidiary T2 Technology, had effective control over Jinyou and was considered the primary beneficiary of Jinyou. In September 2008, Jinyou acquired an ICP license required for the operation of our Asian online game and services business in the PRC and the agreements entered into by and among T2 Technology, Jinyou and the equity interest owners of Jinyou became effective. Accordingly, the financial results of Jinyou were included in the accompanying consolidated financial statements starting from September 2008 through July 1, 2010.

As a result of a dispute that arose in July 2010 with T2CN's former Chief Executive Officer, we had been prevented from obtaining the financial information necessary to report the financial results of T2CN, and we had effectively lost control over T2CN's financial reporting process. Therefore, we deconsolidated T2CN's financial results with effect from July 1, 2010. As a result, we also ceased treating T2 Entertainment, T2 Advertisement and Jinyou as our variable-interest entities. See note 5 to our consolidated financial statements for additional information.

The net assets, total assets and total liabilities in the aggregate of T2 Entertainment, T2 Advertisement and Jinyou were approximately US\$2.5 million, US\$20.9 million and US\$18.4 million, respectively, as of July 1, 2010 (the date of deconsolidation). For the period from January to June 2010, total revenue and net income in the aggregate of T2 Entertainment, T2 Advertisement and Jinyou recorded in our consolidated financial statements were as follows:

|               | <b>2010</b><br><b>(in US\$<br/>thousands)</b> |
|---------------|---|
| Total revenue | \$ 10,126                                     |
| Net income    | \$ 834  |

***Consolidation of UIM***

Through the date of the sale of 60 percent of the gaming software and service business to BetClic in April 2010, we had a software license and support service contract with UIM to provide Internet software and support services for UIM's online gaming operations. The contract allowed us to charge UIM a percentage of its gross receipts resulting from UIM's online gaming operations. The percentage of gross receipts varied depending upon the software and support services provided to UIM. We analyzed our contractual relationships with UIM and determined that we were the primary beneficiary of UIM. As a result of such determination, we had incorporated the financial results of UIM into our consolidated financial statements, even though we did not own any of UIM's equity. In connection with the sale to BetClic, we purchased 100 percent of the ownership in UIM from its shareholders for US\$400 thousand and adjusted additional paid-in capital and noncontrolling interest by approximately US\$178 thousand and US\$(578) thousand, respectively. Subsequent to the sale, UIM became dormant.

For the period from January to March 2010, total revenue and net income of UIM recorded in our consolidated financial statements were as follows:

|               | <b>2010</b><br><b>(in US\$</b><br><b>thousands)</b> |
|---------------|---|
| Total revenue | \$ 25,820   |
| Net income    | \$ 1,514  |



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### ***Share Repurchase Program***

On May 20, 2011, our board of directors approved an US\$11 million share repurchase program of GigaMedia's common stock. Under the terms of the share repurchase program, GigaMedia could repurchase up to US\$11 million worth of its issued and outstanding shares during the period starting from June 1, 2011 to November 30, 2011. The repurchases could be made from time to time on the open market at prevailing market prices pursuant to a Rule 10b5-1 plan, subject to restrictions relating to volume, pricing and timing. The timing and extent of any repurchases depended upon market conditions, the trading price of GigaMedia's shares and other factors. This share repurchase program was implemented in a manner consistent with market conditions, in the interests of our shareholders, and in compliance with GigaMedia's securities trading policy and relevant Singapore and U.S. laws and regulations. During 2011, repurchases under this program amounted to approximately 5.6 million shares at a cost of US\$6.0 million. All of the shares repurchased under this program were cancelled by the end of 2011.

### ***Impairment Loss Related to Underperforming Game Projects in Our Asian Online Game and Service Business***

#### **2010 Impairment Loss**

We recorded an impairment loss of approximately US\$4.7 million due to certain underperforming game projects and of approximately US\$22.2 million due to the deconsolidation of T2CN within our Asian online game and service business in our consolidated financial statements for the year ended December 31, 2010 as follows:

- 1) US\$2.3 million impairment loss on goodwill from the acquisition of IAHGAMES. The goodwill had a carrying amount of US\$12.2 million which was written down to its estimated fair value of US\$9.9 million, resulting in the impairment charge of US\$2.3 million. Goodwill is valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs.
- 2) US\$870 thousand impairment loss on prepaid licensing and royalty fees, which was related to certain licensed games that we stopped operating or for which the carrying amounts were determined not to be recoverable due to lower than expected performances. Prepaid licensing and royalty fees are valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs.
- 3) US\$1.3 million impairment loss on intangible assets for capitalized software costs to reflect a full provision relating to certain projects that we have ceased to further develop.
- 4) US\$278 thousand impairment loss on fixed assets, which was related to servers used in certain impaired licensed games or internally developed games. Fixed assets are valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs; and
- 5) US\$22.2 million impairment loss on the deconsolidation of T2CN. Given we had been prevented from obtaining the financial information necessary to report the financial results of T2CN, and we effectively lost control over a majority of T2CN's assets and its financial reporting process, we decided to completely write-off both the Company's investment of US\$22.2 million and its advances of US\$1.4 million to the T2CN Operating Entities as of December 31, 2010. The write off of advances of US\$1.4 million was included in bad debt expense.

#### **2011 Impairment Loss**

We recorded an impairment loss of approximately US\$8.3 million due to certain underperforming game projects within our Asian online game and service business in our consolidated financial statements for the year ended December 31, 2011 as follows:

- 1) US\$5.1 million impairment loss on goodwill from the acquisition of IAHGAMES. The goodwill had a carrying amount of US\$12.2 million which was written down to its estimated fair value of US\$9.9 million as of December 31, 2010, and fully written down to US\$0 as of December 31, 2011, after the reversal of a contingent liability recorded in connection with the acquisition of IAHGAMES for US\$5.9 million, resulting in an impairment charge of US\$4.0 million in 2011, which is included in operating expenses in our consolidated statements of income (loss). Goodwill from the acquisition of OneNet Co., Ltd., an investee of IAHGAMES, with a carrying amount of US\$1.0 million was fully written down to US\$0 as of December 31, 2011, resulting in an impairment charge of US\$1.0 million in 2011. Goodwill is valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs.

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2) US\$619 thousand impairment loss on prepaid licensing and royalty fees (of which US\$372 thousand related to Shanghai JIDI is reclassified to loss from discontinued operations), which was related to certain licensed games that we stopped operating or for which the carrying amounts were determined not to be recoverable due to lower than expected performances. Prepaid licensing and royalty fees are valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs; and

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3) US\$2.6 million impairment loss on intangible assets for capitalized software costs and favorable lease rights, reflecting a full provision relating to certain projects that we have ceased to further develop.

### **2012 Impairment Loss**

We recorded an impairment loss of approximately US\$13.2 million due to decreased forecasts within our Asian online game and service business in our consolidated financial statements for the year ended December 31, 2012 as follows:

1) US\$12.5 million impairment loss on goodwill from the acquisition of FunTown. Goodwill from the acquisition of FunTown, which constitutes our Asian online game and service business, was written down to its estimated fair value of US\$16.9 million as of December 31, 2012, resulting in an impairment charge of US\$12.5 million in 2012, which is included within operating expenses in our consolidated statements of income (loss). As a result of the slowdown in the PC-based online game market and our repositioning of FunTown to focus on market growth in browser/mobile games in an emerging multi-platform market, we estimated that the fair value of our Asian online game and service business had decreased and, as a result, impaired the goodwill related to FunTown as of December 31, 2012. The impairment charge was determined by our estimates of future cash flows from the FunTown business which have been reduced due to our change in strategic focus to self-developed casual games versus licensed MMOs and the slowdown in PC-based online games market where we are currently positioned, indicating that the original carrying amount of the goodwill from the acquisition of FunTown could not be fully recovered as of December 31, 2012. Goodwill is valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs.

2) US\$702 thousand impairment loss on prepaid licensing and royalty fees, which was related to certain licensed games that we stopped operating or for which the carrying amounts were determined not to be recoverable due to lower than expected performances. Prepaid licensing and royalty fees are valued on a nonrecurring basis when impairment exists, using a discounted cash flow model to determine fair value, incorporating available market discount information, our estimate for liquidity risk and other cash flow model related assumptions based on unobservable inputs; and

3) US\$15 thousand impairment loss on intangible assets for capitalized software costs, reflecting a full provision relating to certain projects that we have ceased to further develop.

### ***Impairment Loss on Marketable Securities and Investments***

As a result of unsuccessful investments made by previous management in game studios and companies, we recognized impairment loss on marketable securities and investments of US\$4.7 million, US\$13.3 million and US\$1.2 million in 2010, 2011 and 2012, respectively. The major impairments are listed below:

#### **2010 Impairment Loss on Marketable Securities and Investments**

1) In 2008, we made an investment in preferred shares of Access China of US\$3 million. As a result of deteriorating earnings and inability to meet its projections and forecasts, we fully wrote off our investment in Access China in 2010.

2) In 2010, we made an investment in preferred shares of Possibility Space Limited ( PSI ) of US\$1.5 million, which ceased operations in December 2010. We fully wrote off our investment in PSI in 2010.

#### **2011 Impairment Loss on Marketable Securities and Investments**

1) In 2009 we made an investment in common shares of Numen Soft Co., Ltd. ( Numen Soft ) of US\$679 thousand. As a result of deteriorating earnings and inability to meet its projections and forecasts, we fully wrote off our investment in Numen Soft in 2011.

2)

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In 2010, we acquired from IAHGames 100 percent of common shares of Spring Asia Limited which owns 30 percent interest in Game First International Corporation ( GFI ) in connection with our acquisition of a controlling financial interest in IAHGames. The carrying amount of this investment was US\$15.1 million as of December 31, 2011. The investment was written down to its estimated fair value of US\$2.5 million, resulting in an impairment charge of US\$12.6 million in 2011.

### 2012 Impairment Loss on Marketable Securities and Investments

- 1) In 2009 we made an investment in common shares of Gorilla Banana Entertainment Corp. ( GBE ) of US\$700 thousand. As a result of accumulated loss, inability to meet its projections and forecasts, and cash shortage, we fully wrote off our investment in GBE in 2012.
- 2) In 2007, we made an investment in common shares of Soft Star Entertainment Inc. ( SoftStar ) of approximately US\$1.9 million through a private placement. As a result of deteriorating earnings and considering the resulting lack of liquidity, we wrote down this investment to its estimated fair value of US\$1.6 million, resulting in an impairment charge of US\$493 thousand in 2012.

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### **Subsequent Events**

Receivables from the sale of 100% of our Spring Asia Limited shares totaled US\$3 million and are due in four equal installments from IAHGAMES. As of April 30, 2013, IAHGAMES has only paid the first installment in the amount of US\$750,000, and has defaulted on the remaining three installments. We have provided IAHGAMES sufficient payment demand notices, and also granted IAHGAMES a 90-day curing period for each defaulted payment following the due dates for each of the respective installments. Additionally, we have also provided IAHGAMES notices upon the expiration of each of the 90-day curing periods of our intention to enforce re-possessing rights on the proportionate shares held by the escrow agent. The curing period of the last installment will expire on July 2, 2013.

We entered into the IAH Settlement Agreement, dated April 17, 2013, with IAHGAMES, MCIL, Spring Asia, and ROTW. Pursuant to the terms of the IAH Settlement Agreement, IAHGAMES and/or ROTW agreed to pay us US\$2.258 million (inclusive of interest) to fulfill IAHGAMES obligations under the Spring Asia Share Purchase Agreement. Pursuant to the terms of the IAH Settlement Agreement, MCIL also agreed to purchase all of our remaining shares in IAHGAMES at a purchase price of US\$1 million, by exercising its call option under the IAH Share Purchase Agreement on April 15, 2013. The parties to the IAH Settlement Agreement agreed that the consideration for such transactions will be paid to us on or before May 2, 2013.

### **Critical Accounting Policies**

The discussion and analysis of our financial condition and results of operations are derived from our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the U.S., or U.S. GAAP. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities as of the date of the consolidated financial statements. We continually evaluate our estimates and assumptions, which are based on historical experience and other various factors that we believe are reasonable under the circumstances. The results of these estimates and assumptions form the basis for making judgments about the carrying values of certain assets and liabilities. Our actual results could differ significantly from those estimates under different assumptions and conditions. We believe that the following discussion addresses the most critical accounting policies applicable to our Company, which are those that are most important to the portrayal of the financial condition and results of operations of our Company, and require management's most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

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### ***Discontinued Operations***

In June 2012, our board of directors approved a plan to liquidate and dissolve JIDI and Shanghai JIDI, a variable-interest entity controlled through a series of contractual arrangements. Therefore the results of these entities are reported as discontinued operations for all periods presented. (See note 6 to our consolidated financial statements for additional information.)

### ***Consolidation***

The consolidated financial statements include the accounts of us and our wholly-owned, majority-owned and majority-controlled subsidiaries after elimination of all inter-company accounts and transactions. In addition, the accounts of our Company's VIEs as defined by the FASB Accounting Standards Codification are included in the consolidated financial statements. See note 3 to our consolidated financial statements for additional information. The accounting policies for other less than majority-owned investments are described in note 1 to our consolidated financial statements in the paragraphs headed "Marketable Securities" and "Investments".

### ***Foreign Currency Translation***

The consolidated financial statements of our Company and our subsidiaries have been reported in U.S. dollars. Assets and liabilities denominated in non-U.S. currency are translated to U.S. dollars at year-end exchange rates. Income and expense items are translated at weighted-average rates of exchange prevailing during the year. Cumulative translation adjustments resulting from this process are charged or credited to other comprehensive income within equity. Gains and losses on foreign currency transactions are included in other income and expenses.

### ***Acquisitions***

Our Company accounts for its business acquisitions using the acquisition method as required by the FASB. Under this method, our Company recognizes and measures the identifiable assets acquired, the liabilities assumed and any noncontrolling interest at their acquisition-date fair values, with limited exceptions. Acquisition-related costs will be generally expensed as incurred.

### ***Revenue Recognition***

Our Company recognizes revenue when persuasive evidence of an arrangement exists, delivery occurs or services are rendered, the sales price is fixed or determinable and collectability is reasonably assured. We present the sales taxes assessed by governmental authorities on our revenue transactions on a net basis in our consolidated financial statements.

Our Company enters into multiple-element revenue arrangements, which may include any combination of services, software, and/or products. To the extent that a deliverable in a multiple-element arrangement is subject to specific accounting guidance, whether and/or how to separate multiple deliverable arrangements into separate units of accounting (separability) and how to allocate the arrangement consideration among those separate units of accounting (allocation) for that deliverable is accounted for in accordance with such specific guidance.

In addition to the aforementioned general policies, the following are the specific revenue recognition policies for each major category of revenue.

#### ***Asian Online Game and Service Revenues***

Asian online game and service revenues are related to our Asian online game and service business that operates play-for-fun games online to players across Asia.

Asian online game revenues are earned through the sale of online game points, prepaid cards, game packs, through the sublicensing of certain games to distributors and through licensing fee revenues. Virtual online game points are sold to distributors or end-users who can make the payments through credit cards, Internet ATMs or telecommunication service operators. Physical prepaid cards and game packs are sold through distributors and convenience stores. Proceeds from sales of physical cards and game packs, net of sales discounts, and online game points are deferred when received and revenue is recognized upon the actual usage of the playing time or in-game virtual items by the end-users; over the estimated useful life of virtual items; or when the sold game points expire and can no longer be used to access the online games or products in accordance with our published game points expiration policy. Sublicensing revenues from the distributors are recognized based on end-users activation to the game system and when the performance obligations have been completed. Licensing fee revenues are recognized when the

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delivery of licensed products has occurred and the fee is fixed or determinable.

We report sales of virtual online game points and licensing fee revenues on a gross basis. In the sales of virtual online game points and game licenses, we act as principal and we have latitude in establishing price. Fixed percentage fees retained by service providers for payment processing related to our online game services are recognized as cost of online game revenues. We report sublicensing revenues on a net basis. In the sublicense agreements, we act as agent and the distributors are responsible for the operating and the marketing.

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Asian online game and service revenues also include revenues derived from online advertising arrangements, sponsorship arrangements, or a combination of both. These service arrangements allow advertisers to place advertisements on particular areas of our Company's websites and online game platforms over a stated period of time. Service revenues from online advertising arrangements are recognized ratably over the displayed period of the contract when the collectability is reasonably assured.

### *Gaming Software and Service Revenues*

Prior to our sale of a 60 percent interest in our online gaming software and service business in April 2010, gaming software and service revenues were related to software products we developed and licensed and support services we provided for online real-money gaming solutions and applications. Subsequent to the sale, the remaining 40 percent ownership interest that we retained in the gaming software and service business was accounted for under the equity method starting from April 2010 through July 2012; therefore, no revenue directly from gaming software and service business was subsequently recorded.

### *Deferred Revenues*

Deferred revenues are included in other current liabilities, and consist of the prepaid income related to our Asian online game and service business.

### *Operating Costs*

Operating costs primarily consist of processing costs, online game royalties, bandwidth, production costs for prepaid game cards and game packs, amortization of intangible assets, customer service department costs, depreciation, maintenance and other overhead expenses directly attributable to our online games.

### *Prepaid Licensing and Royalty Fees*

Our Company, through our subsidiaries, routinely enters into agreements with licensors to acquire licenses for using, marketing, distributing, selling and publishing multi-player online games.

Prepaid licensing fees paid to licensors are capitalized when technological feasibility is achieved, and amortized on a straight-line basis over the shorter of the estimated useful economic life of the relevant online game or license period, which is usually within two to five years. The annual amortization is modified if the amount computed using the ratio that current gross revenues for a game license bear to the total of current and anticipated future gross revenues for that game license is greater than the amount computed using the straight-line method.

Prepaid royalty fees and related costs are initially deferred when paid to licensors and recognized as operating costs in the period in which the related online game revenue is recognized.

### *Fair Value Measurement*

Our Company generally determines or calculates the fair value of financial instruments using quoted market prices in active markets when such information is available or using appropriate present value or other valuation techniques, such as discounted cash flow analyses, incorporating adjusted available market discount rate information and our Company's estimates for non-performance and liquidity risk. These techniques rely extensively on the use of a number of assumptions, including the discount rate, credit spreads, and estimates of future cash flows. See note 10 to our consolidated financial statements for additional information.

### *Marketable Securities*

All of our Company's investments in marketable securities are classified as available-for-sale. These marketable securities are stated at fair value with any unrealized gains or losses recorded in accumulated other comprehensive income (loss) within equity until realized.

Other-than-temporary impairments, if any, are charged to non-operating expense in the period in which the loss occurs. In determining whether an other-than-temporary impairment has occurred, our Company primarily considers, among other factors, the length of the time and the extent to which the fair value of an investment has been at a value less than cost. When an other-than-temporary loss is recorded, the fair value of the investment becomes the new cost basis of the investment and is not adjusted for subsequent recoveries in fair value. Realized gains and losses also are included in non-operating income and expense in the consolidated statements of income (loss). See note 10 to our consolidated financial



statements for additional information.

***Investments***

Equity investments in non-publicly traded securities of companies over which our Company has no ability to exercise significant influence are accounted for under the cost method.

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Equity investments in companies over which our Company has the ability to exercise significant influence but does not hold a controlling financial interest are accounted for under the equity method and our Company's income or loss on equity method investments is recorded in non-operating income or expenses. The difference between the cost of the acquisition and our Company's share of the fair value of the net identifiable assets is recognized as goodwill and is included in the carrying amount of the investment. When our Company's carrying value in an equity method investee is reduced to zero, no further losses are recorded in our consolidated financial statements unless our Company guaranteed obligations of the investee or has committed to additional funding. When the investee subsequently reports income, our Company will not record its share of such income until it equals the amount of its share of losses not previously recognized.

Unrealized losses that are considered other-than-temporary, if any, are charged to non-operating expenses. Realized gains and losses, measured against carrying amount, are also included in non-operating income and expenses. See note 10 to our consolidated financial statements for additional information.

### ***Allowance for Doubtful Accounts***

An allowance for doubtful accounts is provided based on an evaluation of the collectability of accounts receivable, and other receivables. An allowance for doubtful accounts is also provided, when considered necessary, for loans receivable. We review the collectability of loans receivable on an individual basis and the evaluation primarily consists of an analysis based upon current information available about the borrower.

For those accounts in which a loss is probable, we record a specific reserve. The receivable is written off against the allowance when our Company believes the uncollectability of the receivable is confirmed. Subsequent recoveries, if any, are credited to the allowance.

### ***Intangible Assets and Goodwill***

Intangible assets with finite lives are amortized by the straight-line method over their estimated useful lives, ranging from three to nine years. Intangible assets with indefinite useful lives are not amortized. Goodwill is not amortized.

### ***Impairment of Intangible Assets, Goodwill and Long-Lived Assets***

Potential impairment of goodwill is tested annually or sooner when circumstances indicate an impairment may exist, using a fair-value approach at the reporting unit level. A reporting unit is the operating segment, or a business, which is one level below that operating segment (the component level) if discrete financial information is prepared and regularly reviewed by management at the segment level. Components are aggregated as a single reporting unit if they have similar economic characteristics. Pursuant to an updated guidance issued by the FASB in September 2011, in connection with our goodwill impairment test for the year ended December 31, 2012, we first assessed qualitative factors as a basis for determining whether it is necessary to perform the two-step goodwill impairment test.

Potential impairment of intangible assets with indefinite useful lives is evaluated, at the reporting unit level, at least annually, or whenever events or changes in circumstances indicate that the carrying value of an asset might not be recoverable from its related future discounted cash flows. Impairment is measured as the difference between the carrying amounts and the fair value of the assets, and is recognized as a loss from operations.

Potential impairment of long-lived assets other than goodwill and intangible assets not being amortized, is evaluated, at least annually or whenever events or changes in circumstances indicate that the carrying value of an asset might not be recoverable from its related future undiscounted cash flows. If such assets are considered to be impaired, the impairment to be recognized is measured by the extent to which the carrying amount of the assets exceeds the fair value of the assets. When impairment is identified, the carrying amount of the asset is reduced to its estimated fair value, and is recognized as a loss from operations.

See note 10 to our consolidated financial statements for additional information.

### ***Software Cost***

Costs to develop our gaming software and Asian online game products are capitalized after technological feasibility has been established, and when the product is available for general release to customers, costs are expensed. Costs incurred prior to the establishment of technological feasibility are expensed when incurred and are included in product development and engineering expenses. Capitalized amounts are amortized using the straight-line method, which is applied over the estimated useful economic life of the software, ranging from three to five years. The annual amortization is modified if the amount computed using the ratio that current gross revenues for a product bear to the total of current and

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anticipated future gross revenues for that product is greater than the amount computed using the straight-line method.

We capitalize certain costs incurred to purchase or to internally create and implement internal-use computer software, which includes software coding, installation, testing and certain data conversion. These capitalized costs are amortized on a straight-line basis over the shorter of the useful economic life of the software or its contractual license period, which range from three to five years.

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### ***Share-Based Compensation***

Share-based compensation represents the cost related to share-based awards granted to employees. We measure share-based compensation cost at the grant date, based on the estimated fair value of the award. Share-based compensation is recognized for the portion of the award that is ultimately expected to vest, and the cost is amortized on a straight-line basis (net of estimated forfeitures) over the vesting period. Our Company estimates the fair value of stock options using the Black-Scholes valuation model. The cost is recorded in operating costs and operating expenses in the consolidated statements of income (loss) based on the employees' respective function.

For shares and stock options granted to non-employees, we measure the fair value of the equity instruments granted at the earlier of the performance commitment date or when the performance is completed.

### ***Income Taxes***

The asset and liability method is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on the differences between financial reporting and tax bases of assets and liabilities. We recognize the tax benefit from the purchase of equipment and technology, research and development expenditures, employee training, and certain equity investments using the flow-through method. Net operating loss carryforwards and investment credits are measured using the enacted tax rate and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established when necessary to reduce deferred tax assets to the amount that will more-likely-than-not be realized. In assessing the likelihood of realization, management considers estimates of future taxable income.

In addition, we recognize the financial statement impact of a tax position when it is more-likely-than-not that the position will be sustained upon examination. If the tax position meets the more-likely-than-not recognition threshold, the tax effect is recognized at the largest amount of the benefit that has greater than a 50 percent likelihood of being realized upon ultimate settlement. The interest and penalties are reflected as income taxes expenses in the consolidated financial statements.

### ***Reclassifications***

The presentation of certain amounts in our 2011 consolidated financial statements have been reclassified to conform to the presentation in our consolidated financial statements as of and for the year ended December 31, 2012.

### ***Recent Accounting Pronouncements***

In February 2013, Accounting Standards Codification (ASC) guidance was issued related to items reclassified from Accumulated Other Comprehensive Income. The new standard requires either in a single note or parenthetically on the face of the financial statements: (i) the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and (ii) the income statement line items affected by the reclassification. The update is effective for our fiscal year beginning January 1, 2013 with early adoption permitted. We do not expect the updated guidance to have a significant impact on our consolidated financial position, results of operations or cash flows.

In July 2012, the FASB issued updated guidance that simplifies the impairment test for intangible assets not subject to amortization. For its annual and interim impairment test for intangible assets, an entity may first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the quantitative impairment test. This update is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. However, early adoption is permitted, if an entity's financial statements for the most recent annual or interim period have not yet been issued. We adopted the updated guidance for our annual impairment test for intangible assets not subject to amortization in 2012. The adoption of this guidance had no impact on our consolidated financial position, results of operations, or cash flows.

In June 2011, the ASC guidance was issued related to comprehensive income. Under the updated guidance, an entity will have the option to present the total of comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In addition, the update required certain disclosure requirements when reporting other comprehensive income. The update does not change the items reported in other comprehensive income or when an item of other comprehensive income must be reclassified to income. We adopted the new guidance and its deferral and opted to present the total of comprehensive income in two separate but consecutive statements. The adoption of this guidance had no impact on our consolidated financial position, results of operations or cash flows.

### ***Taxation***

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Our major tax jurisdictions are located in Taiwan, the PRC and Singapore.

The corporate income tax rate in Taiwan is 17 percent effective from 2010. In addition to the corporate income tax rate, all retained earnings generated beginning January 1, 1998 by our subsidiaries under Taiwan law and not distributed to us as dividends in the following year are assessed a 10 percent retained earnings tax. This rule applies primarily to our FunTown online games portal, whose principal operating entities are incorporated under Taiwan law.

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On January 1, 2006, the Taiwanese government enacted the AMT Act. Taxes imposed under the AMT Act are supplemental tax payable if the income tax payable pursuant to the R.O.C. Income Tax Act is below the minimum amount prescribed under the AMT Act. The AMT rate for business entities is 10 percent. The taxable income for calculating the AMT includes most income that is exempted from income tax under various legislation such as tax holidays and investment tax credits. For example, gains on disposal of marketable securities from our Taiwan-based entities were exempt from income tax based on Taiwan tax laws prior to the AMT Act. However, such gains will need to be included for the purpose of calculating the AMT.

The statutory enterprise income tax rate in the PRC is 25 percent unless the entities qualify under certain limited exceptions. Our Asian online games in the PRC applied this income tax rate before we ceased our operations in the PRC.

The corporate income tax rate in Singapore is 17 percent, which applies primarily to IAHGames acquired in July 2010.

## **Discussion of Results of Operations**

### ***Factors Affecting Our Performance***

We believe that the following are the principal factors affecting our results of operations:

*Acquisitions and disposals.* We have made several significant acquisitions and dispositions of businesses during the past several years, and may enter into additional acquisition and disposition transactions in the future. Past acquisitions and dispositions have had a significant impact on our results of operations over the past several years, and if we engage in such transactions in the future, the nature, amounts and timing of our revenues, expenses and cash flows and the nature and amounts our assets and liabilities are likely to be materially affected.

*Development of cloud computing and online games industries.* We began developing a new cloud computing business in the second half of 2012. The business launched in early April 2013. The cloud computing and online games industries are in relatively early stages of development. We believe that our results of operations are likely to be affected by developments in these industries, including:

the development and regulation of these industries;

our adaptation to technological change;

changing consumer preferences;

legal development affecting these industries; and

general economic conditions in the markets where we or our licensees operate.

*Competition.* Our online games business operates in an extremely competitive industry and our cloud computing business may face strong future industry competition as the cloud computing industry grows in Asia. Our Asian online games business is characterized by rapid technological change and we face significant and intense competition from online game software design houses, application service providers and casual games operators. Our nascent cloud computing business also faces rapid technological change and potential intense future competition from major telecommunication service operators and Internet application providers.

*Divestiture of Gaming Software and Service Business.* When we sold a 60 percent ownership interest in our gaming software and service business on April 8, 2010, we ceased to consolidate its financial results and no longer have revenue from the gaming software and service business from April 2010 onwards. Our remaining ownership interest in the gaming software and service business was accounted for under the equity method until we sold such interest in July 2012.

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For each of our businesses, we cannot assure you that we will be successful in adapting to technological developments and achieving widespread acceptance of our services before our competitors offer services similar to our current or prospective offerings. As a consequence, we may lose our existing customers and not expand our client base, which would have a material adverse effect on our revenues and financial condition.

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The table below presents, for the periods indicated, information regarding certain revenues and expense items for our consolidated operations.

|   | For the Year Ended December 31, |                           |                                |                           |                                |                           |
|---|---------------------------------|---------------------------|--------------------------------|---------------------------|--------------------------------|---------------------------|
|   | 2010                            |                           | 2011                           |                           | 2012                           |                           |
|   | Amount in<br>US\$<br>thousands  | % of<br>total<br>revenues | Amount<br>in US\$<br>thousands | % of<br>total<br>revenues | Amount<br>in US\$<br>thousands | % of<br>total<br>revenues |
| <b>OPERATING REVENUES</b>   |                                 |                           |                                |                           |                                |                           |
| Gaming software and service revenues                                    | 25,820                          | 39.9                      |                                |                           |                                |                           |
| Asian online game and service revenues                                  | 38,862                          | 60.1                      | 34,367                         | 100.0                     | 27,470                         | 100.0                     |
| Total operating revenues  | 64,682                          | 100.0                     | 34,367                         | 100.0                     | 27,470                         | 100.0                     |
| <b>OPERATING COSTS</b>  |                                 |                           |                                |                           |                                |                           |
| Cost of gaming software and service revenues                            | 4,010                           | 6.2                       |                                |                           |                                |                           |
| Cost of Asian online game and service revenues                          | 17,103                          | 26.4                      | 14,413                         | 41.9                      | 11,388                         | 41.5                      |
| Total operating costs   | 21,113                          | 32.6                      | 14,413                         | 41.9                      | 11,388                         | 41.4                      |
| Gross profit  | 43,569                          | 67.4                      | 19,954                         | 58.1                      | 16,082                         | 58.6                      |
| <b>OPERATING EXPENSES</b>   |                                 |                           |                                |                           |                                |                           |
| Product development and engineering expenses                            | 7,301                           | 11.3                      | 1,956                          | 5.7                       | 1,471                          | 5.4                       |
| Selling and marketing expenses  | 21,589                          | 33.4                      | 10,079                         | 29.3                      | 8,377                          | 30.5                      |
| General and administrative expenses                                     | 31,780                          | 49.1                      | 18,101                         | 52.7                      | 13,384                         | 48.7                      |
| Bad debt expense  | 1,639                           | 2.5                       | 1,820                          | 5.3                       | 169                            | 0.6                       |
| Impairment loss on property, plant, and equipment                       | 278                             | 0.4                       |                                |                           |                                |                           |
| Impairment loss on goodwill   | 2,255                           | 3.5                       | 5,097                          | 14.9                      | 12,489                         | 45.5                      |
| Impairment loss on prepaid licensing and royalty fees                   | 1,330                           | 2.1                       | 2,583                          | 7.5                       | 15                             |                           |
| Impairment loss on intangible assets                                    | 870                             | 1.3                       | 247                            | 0.7                       | 702                            | 2.6                       |
| Impairment loss on deconsolidation of T2CN                              | 22,234                          | 34.4                      |                                |                           |                                |                           |
| Other   | 1,989                           | 3.1                       |                                |                           | 49                             | 0.2                       |
| Total operating expenses  | 91,265                          | 141.1                     | 39,883                         | 116.1                     | 36,656                         | 133.5                     |
| Loss from operations  | (47,696)                        | (73.7)                    | (19,929)                       | (58.0)                    | (20,574)                       | (74.9)                    |
| NON-OPERATING INCOME (EXPENSES)   | 56,364                          | 87.1                      | (47,706)                       | (138.8)                   | 7,649                          | 27.8                      |
| <b>INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE<br/>INCOME TAXES</b> |                                 |                           |                                |                           |                                |                           |
| INCOME TAX BENEFIT (EXPENSE)  | (7,260)                         | (11.2)                    | 245                            | 0.7                       | (671)                          | (2.4)                     |
| INCOME (LOSS) FROM CONTINUING OPERATIONS                                | 1,408                           | 2.2                       | (67,390)                       | (196.1)                   | (13,596)                       | (49.5)                    |
| INCOME (LOSS) FROM DISCONTINUED OPERATIONS -NET<br>OF TAX               | (128)                           | (0.2)                     | (4,188)                        | (12.2)                    | (2,521)                        | (9.2)                     |



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|   |       |     |          |         |          |        |
|---|-------|-----|----------|---------|----------|--------|
| NET INCOME (LOSS)   | 1,280 | 2.0 | (71,578) | (208.3) | (16,117) | (58.7) |
| LESS: NET LOSS ATTRIBUTABLE TO NONCONTROLLING<br>INTEREST AND SUBSIDIARY PREFERRED SHARES | 1,370 | 2.1 | 366      | 1.1     | 827      | 3.0    |
| NET INCOME (LOSS) ATTRIBUTABLE TO GIGAMEDIA   | 2,650 | 4.1 | (71,212) | (207.2) | (15,290) | (55.7) |

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The key items included in our income statement are:

**OPERATING REVENUES.** Our operating revenues consist of revenues from our former gaming software and service business and our current Asian online game and service business. Until April 8, 2010, revenues from the gaming software and service business included revenues of UIM, our licensee, from providing and promoting online games of skill and chance. Software licensing and support services revenues received by our subsidiary, CESL, from UIM have been eliminated in consolidation. When we sold a 60 percent ownership interest in our gaming software and service business on April 8, 2010, we deconsolidated its financial results and no longer had revenue from gaming software and service business from April 2010 onwards. Our remaining ownership interest in the gaming software and service business was accounted for under the equity method until we sold such interest in July 2012. Asian online game and service revenues are related to our online games business in Asia and are collected through the sale of online game points, pre-paid cards and game packs, and through licensing fee revenues.

**OPERATING COSTS.** Operating costs consist primarily of gaming software and online game processing costs, online game royalties, production costs for prepaid game cards and game packs, amortization of intangible assets, customer service department costs, operational department costs, depreciation, maintenance and other overhead expenses directly attributable to the provision of gaming software and service and Asian online game and services.

**OPERATING EXPENSES.** Operating expenses include product development and engineering expenses, selling and marketing expenses, general and administrative expenses, bad debt expenses and impairment losses.

**NON-OPERATING INCOME (EXPENSES).** Non-operating income and expenses consist of interest income and expenses, gain or loss on sales of marketable securities, foreign exchange gain or loss, gain or loss on disposal of property, plant and equipment, loss on equity method investments, gain or loss on deconsolidation of business units, impairment loss on marketable securities and investments, and gain or loss on fair value changes of warrant derivatives.

**INCOME TAX EXPENSES (BENEFIT).** Taxes include current income tax in various jurisdictions in which our subsidiaries operate and deferred tax expenses related to temporary tax assets or liabilities that arise due to the timing differences between book profits and taxable profits that originate in one period and are capable of reversal in one or more subsequent periods. Taxes are measured using the tax rates and laws that have been enacted or subsequently enacted as of the date of the financial statements.

**NONCONTROLLING INTEREST.** Noncontrolling interest represents the portion of net income allocated to the non-controlling voting shares of our majority-owned subsidiaries (T2CN through December 13, 2011, Dragongate Enterprises Limited, and IAHGames through August 15, 2012) as well as UIM, which was consolidated pursuant to the FASB Accounting Standards Codification through March 31, 2010. In May 2005, IAHGames issued redeemable preferred shares, which are redeemable at the option of the investors, and as such these preferred shares are classified as mezzanine equity on our balance sheet, through August 15, 2012.

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The financial information in relation to our business segments is provided net of inter-segment transactions.

**For the Years Ended December 31, 2012 and 2011**

***Consolidated Results of Operations***

**OPERATING REVENUES.** Operating revenues for 2012, all from our Asian online game and service business, declined by approximately 20.0 percent to approximately US\$27.5 million from approximately US\$34.4 million in 2011. The decrease was primarily due to a decrease of approximately US\$2.7 million in revenue from FunTown and the sale of our 60 percent ownership interest in IAHGames in August 2012. As a result, we deconsolidated the results of IAHGames from August 2012 onwards and do not expect to generate revenue from IAHGames going forward. Therefore, revenue from IAHGames declined to US\$4.2 million in 2012 from approximately US\$8.4 million in 2011, which accounted for 15.3 percent of our total revenues in 2012.

**OPERATING COSTS.** Operating costs in 2012 and 2011, all from our Asian online game and service business, decreased by approximately US\$3.0 million, or 21.0 percent, to approximately US\$11.4 million in 2012 from approximately US\$14.4 million in 2011. The decrease in total operating costs was mainly due to a US\$3.1 million or 47.7 percent, decrease in operating costs in IAHGames as a result of its deconsolidation from August 2012.

**GROSS PROFIT.** Gross profit decreased by approximately 19.4 percent to approximately US\$16.1 million in 2012 from approximately US\$20.0 million in 2011. The decrease in consolidated gross profit mainly resulted from decrease in gross profit from IAHGames as a result of its deconsolidation from August 2012.

**OPERATING EXPENSES.** Total operating expenses decreased by approximately 8.1 percent to approximately US\$36.7 million in 2012 from approximately US\$39.9 million in 2011. The decrease in total operating expenses was mainly due to a US\$13.7 million, or 81.7 percent, decrease in operating expenses from IAHGames as a result of its deconsolidation from August 2012, offset by a US\$11.1 million, or 77.1 percent, increase in operating expenses from FunTown (which primarily resulted from a US\$12.5 million impairment to goodwill).

Consolidated product development and engineering expenses decreased by approximately 24.8 percent in 2012 to approximately US\$1.5 million from US\$2.0 million in 2011. This decrease was mainly due to reduced expenditures in certain online game projects in our Asian online game and service business.

Consolidated selling and marketing expenses decreased by approximately 16.9 percent to approximately US\$8.4 million in 2012 from US\$10.1 million in 2011, primarily due to an decrease of US\$1.1 million, or 50.9 percent, in selling and marketing expenses as a result of the deconsolidation of IAHGames from August 2012.

Consolidated general and administrative expenses decreased by approximately US\$4.7 million, or 26.1 percent, to approximately US\$13.4 million in 2012 from US\$18.1 million in 2011, primarily due to a US\$3.3 million decrease in general and administrative expenses as a result of the deconsolidation of IAHGames from August 2012, and a US\$1.3 million expenditure reduction in general and administrative expenses in FunTown.

Consolidated impairment loss, all in our Asian online games and service business, increased by approximately US\$5.3 million to approximately US\$13.2 million in 2012 from US\$7.9 million in 2011. Total consolidated impairment loss in 2012 was composed of a US\$15 thousand impairment loss on intangible assets for capitalized software costs, a US\$702 thousand impairment loss on prepaid licensing and royalty fees, and a US\$12.5 million impairment loss on goodwill related to FunTown. The total consolidated impairment loss in 2011 was composed of a US\$2.6 million impairment loss on intangible assets for capitalized software costs and favorable lease right, a US\$247 thousand impairment loss on prepaid licensing and royalty fees, and a US\$5.1 million impairment loss on goodwill related to IAHGames.

**OPERATING LOSS.** Operating loss for 2012 was US\$20.6 million as compared to a loss of US\$19.9 million in 2011. The US\$12.7 million decrease in loss was primarily a result of the deconsolidation of IAHGames from August 2012.

**NON-OPERATING INCOME (EXPENSES).** Non-operating income was approximately US\$7.6 million in 2012 compared to non-operating loss of approximately US\$47.7 million in 2011. The non-operating income in 2012 primarily included (1) US\$2.5 million gain on the sale of remaining non-controlling ownership interest in our gaming software and service business, (2) US\$5.7 million gain on the sales of marketable securities, and (3) US\$1.2 million impairment loss on marketable securities and investments. The non-operating loss in 2011 primarily included (1) US\$47.9 million loss on equity method investments, (2) US\$13.3 million impairment loss on marketable securities and investments, (3) US\$6.3 million gain on the sales of marketable securities, (4) US\$4.7 million gain on the sale of ownership interest in T2CN, and (5) US\$2.0

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million gain on recovery of loss on termination of IAHGames initiatives with Blizzard.

**LOSS FROM DISCONTINUED OPERATIONS.** Loss from discontinued operations decreased by approximately US\$1.7 million to approximately US\$2.5 million in 2012 compared to a loss of approximately US\$4.2 million in 2011, primarily due to our discontinuing the operations of JIDI.

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NET LOSS ATTRIBUTABLE TO GIGAMEDIA. Net loss attributable to us for 2012 was approximately US\$15.3 million compared to a loss of approximately US\$71.2 million in 2011 for the reasons mentioned above.

***Business Segment Results***

***Asian Online Game and Service Business***

In July 2012, we entered into agreements to sell a 60 percent ownership interest in IAHGames. Upon the closing of the agreement in August 2012, we deconsolidated the results of IAHGames operations and began accounting for our remaining 20 percent interest under the equity method. See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Acquisition and Divestitures of IAHGames .

In June 2012, our board of directors approved a plan to liquidate and dissolve JIDI, a wholly-owned subsidiary, and Shanghai JIDI, a VIE controlled through a series of contractual arrangements. Results for JIDI and Shanghai JIDI operations are reported as discontinued operations for all periods presented. See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Divestitures of JIDI and Shanghai JIDI .

In addition to these divestitures, financial results of our Asian online game and service business in 2012 were affected by several factors, including but not limited to strong competition from an increase of online games offered on social network platforms.

OPERATING REVENUES. Total operating revenues decreased by approximately US\$6.9 million or 20.0 percent to approximately US\$27.5 million in 2012 from approximately US\$34.4 million in 2011. Such decrease was due to (1) approximately US\$4.2 million or 49.9 percent decrease as a result of the deconsolidation of IAHGames from August 2012, and (2) approximately US\$2.7 million or 10.4 percent decrease related to FunTown operations in Taiwan and Hong Kong, mainly due to declining demand for certain online games.

As of December 31, 2012, FunTown s number of registered users was approximately 21.7 million, representing an increase of 12.4 percent compared with 2011. However, there was a decrease of 17.5 percent in the number of peak concurrent users, compared to 2011, to approximately 36,325, and the number of average monthly active paying accounts was about 59,607, representing a decrease of 25.6 percent compared to 2011. The average revenue per paying user ( ARPU ) was approximately US\$30.39, representing a year-over-year increase of 12.5 percent. The decrease in active paying accounts and increase in ARPU resulted in a decrease in revenue of 10.4 percent in revenue if translated into US dollars.

OPERATING COSTS. Costs of our Asian online game and service revenue decreased by 21.0 percent to approximately US\$11.4 million in 2012 from US\$14.4 million in 2011. The decrease was primarily due to a decrease of approximately US\$3.1 million related to IAHGames, which was deconsolidated from August 2012.

GROSS PROFIT. Gross profit decreased by 19.4 percent to approximately US\$16.1 million in 2012 from US\$20.0 million in 2011. Gross profit margin was approximately 58.5 percent in 2012 compared with 58.1 percent in 2011.

OPERATING EXPENSES. Total operating expenses decreased by approximately US\$2.5 million to approximately US\$28.4 million in 2012 from approximately US\$30.9 million in 2011. The decrease was primarily due to impairment losses of US\$7.7 million related to IAHGames being recorded in 2011, as well as the deconsolidation of IAHGames from August 2012, offset by impairment losses of US\$13.2 million related to FunTown recorded in 2012.

Selling and marketing expenses. Selling and marketing expenses decreased by approximately US\$1.7 million to US\$8.3 million in 2012 from US\$10.0 million in 2011. The decrease was mainly due to the deconsolidation of IAHGames from August 2012 and expenditure reduction in FunTown.

General and administrative expenses. General and administrative expenses incurred in 2012 decreased by approximately US\$4.8 million to US\$5.3 million from US\$10.1 million in 2011. The decrease was mainly due to the deconsolidation of IAHGames from August 2012, and expenditure reduction in FunTown.

Impairment loss. Impairment loss increased by approximately US\$5.3 million to approximately US\$13.2 million in 2012 from US\$7.9 million in 2011. The impairment loss in 2012 was comprised of a US\$15 thousand impairment loss on intangible assets for capitalized software costs, a US\$702 thousand impairment loss on prepaid licensing and royalty fees, and a US\$12.5 million impairment loss on goodwill related to FunTown. The impairment loss in 2011 was comprised of a US\$2.6 million impairment loss on intangible assets for capitalized software costs

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and favorable lease right, a US\$247 thousand impairment loss on prepaid licensing and royalty fees, and a US\$5.1 million impairment loss on goodwill related to IAHGames.

**OPERATING LOSS.** Operating loss in 2012 was US\$12.3 million as compared to US\$10.9 million in 2011. The decrease of loss was due to the aforementioned factors. Operating loss does not reflect certain corporate headquarter expenses.

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NON-OPERATING INCOME (EXPENSES). Non-operating income in 2012 was US\$4.9 million compared to income of US\$1.9 million in 2011. Non-operating income in 2012 mainly included a gain on sales of marketable securities of US\$5.7 million, and an impairment loss of US\$1.2 million on marketable securities and investments. The non-operating income in 2011 mainly included a gain on sales of marketable securities of US\$5.8 million, a gain of US\$4.7 million on disposal of our ownership interest of T2CN, a gain of US\$1.8 million on equity method investments in relation to IAHGames, an impairment loss of US\$13.3 million on marketable securities and investments and a gain of US\$2.0 million on recovery of loss on termination of IAHGames initiatives with Blizzard.

*Gaming Software and Service Business*

On April 8, 2010, we completed the sale of a 60 percent interest in our online gaming software and service business to BetClic. We then ceased to consolidate the financial results of the gaming software and service business. Our remaining non-controlling interest in Everest Gaming was accounted under the equity method until July 2012 when we entered into another agreement with BetClic to sell our remaining ownership interest. See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Divestiture of Gaming Software and Service Business .

OPERATING REVENUES. As a result of our divestiture of our gaming software and service business, no operating revenues were recognized in 2011 and 2012.

OPERATING COSTS. As a result of our divestiture of our gaming software and service business, no costs of our gaming software and service revenues were recognized in 2011 and 2012.

GROSS PROFIT. As a result of our divestiture of our gaming software and service business, no gross profit was recognized in 2011 and 2012.

OPERATING EXPENSES. As a result of our divestiture our of gaming software and service business, total operating expenses decreased by approximately US\$211 thousand, or 44.6 percent, to a credit balance of approximately US\$7 thousand in 2012 from approximately US\$204 thousand in 2011.

Selling and marketing expenses. As a result of our divestiture of our gaming software and service business, no selling and marketing expenses were recognized in 2011 and 2012.

General and administrative expenses. As a result of our divestiture of our gaming software and service business, general and administrative expenses decreased by approximately US\$211 thousand to a credit balance of US\$7 thousand in 2012 from US\$204 thousand in 2011, primarily attributable to reversal of certain accrued expenses.

Product development and engineering expenses. As a result of our divestiture of our gaming software and service business, no product development and engineering expenses were recognized in 2011 and 2012.

OPERATING INCOME (LOSS). The divestiture of our gaming software and service business resulted in an operating income of US\$7 thousand in 2012 compared with operating loss of US\$204 thousand in 2011.

NON-OPERATING INCOME (EXPENSES). Non-operating income increased by approximately US\$52.1 million to approximately income of US\$2.4 million from a non-operating loss of US\$49.8 million in 2011. This increase is primarily because we recorded a US\$49.7 million equity loss for the remaining non-controlling percent interest for the year ended December 31, 2011 and recognized a US\$2.5 million gain from the sale of the remaining interest in our gaming software and service business in July 2012.

**For the Years Ended December 31, 2011 and 2010**

*Consolidated Results of Operations*

OPERATING REVENUES. Operating revenues for 2011 declined by approximately 46.8 percent to approximately US\$34.4 million from approximately US\$64.7 million in 2010. The decrease was primarily due to the sale of our 60 percent ownership interest in our gaming software and service business on April 8, 2010. As a result, we deconsolidated the results of the gaming software and service business from April 2010 onwards and do not expect to generate revenue from the gaming software and service business going forward. Therefore, revenue from our gaming software and service business declined to nil in 2011 from approximately US\$25.8 million in 2010, which accounted for 39.9 percent of our total revenues in 2010. Revenues from our Asian online game and service business decreased by 11.5 percent to approximately US\$34.4

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million, which represented 100 percent of our total revenues in 2011. The decrease was due to a decrease of approximately US\$9.9 million in revenue from T2CN, which was deconsolidated from July 2010. This decrease was partially offset by an increase of approximately US\$2.5 million in revenue from IAHGames, which was consolidated from July 2010, and an increase of approximately US\$2.9 million in revenue from FunTown.



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**OPERATING COSTS.** Operating costs decreased by approximately US\$6.7 million, or 31.7 percent, to approximately US\$14.4 million in 2011 from approximately US\$21.1 million in 2010. The decrease in total operating costs was mainly due to a US\$4.0 million or 100 percent decrease in operating costs in our gaming software and service business as a result of its deconsolidation from April 2010. The operating costs of our Asian online game and service business in 2011 decreased by approximately US\$2.7 million, or 15.7 percent, compared with that in 2010.

**GROSS PROFIT.** Gross profit decreased by approximately 54.2 percent to approximately US\$20.0 million in 2011 from approximately US\$43.6 million in 2010. The decrease in consolidated gross profit resulted from a US\$21.8 million, or 100 percent, and US\$2.7 million, or 12.3 percent, decrease in the gross profits of our gaming software and service business and our Asian online game and service business, respectively.

**OPERATING EXPENSES.** Total operating expenses decreased by approximately 56.3 percent to approximately US\$39.9 million in 2011 from approximately US\$91.3 million in 2010. The decrease in total operating expenses was mainly due to a US\$21.5 million, or 99.1 percent, decrease in operating expenses from our gaming software and service business and a US\$22.4 million, or 41.8 percent, decrease in operating expense from our Asian online game and service business.

Consolidated product development and engineering expenses decreased by approximately 72.6 percent in 2011 to approximately US\$2.0 million from US\$7.3 million in 2010. This decrease was mainly due to the deconsolidation of our gaming software and service business, which resulted in a decrease of US\$3.2 million, or 100 percent, in related product development and engineering expenses, and a US\$2.1 million decrease in product development and engineering expenses in our Asian online game and service business.

Consolidated selling and marketing expenses decreased by approximately 53.3 percent to approximately US\$10.1 million in 2011 from US\$21.6 million in 2010, primarily due to an decrease of US\$12.3 million, or 100 percent, in selling and marketing expenses as a result of the deconsolidation of our gaming software and service business. This decrease was partially offset by an increase of US\$1.1 million, or 11.8 percent, in selling and marketing expenses in our Asian online game and service business related to more promotions and activities held for new games launched in 2011 compared to those in 2010.

Consolidated general and administrative expenses decreased by approximately US\$13.7 million, or 43.0 percent, to approximately US\$18.1 million in 2011 from US\$31.8 million in 2010, primarily reflecting a US\$7.2 million decrease from corporate headquarter expenses due to less legal fees incurred in relation to our dispute with T2CN's former Chief Executive Officer compared to that in 2010, and a US\$6.0 million decrease in general and administrative expenses as a result of the deconsolidation of our gaming software and service business.

Consolidated impairment loss decreased by approximately US\$19.0 million to approximately US\$7.9 million in 2011 from US\$27.0 million in 2010, resulting from a decrease of US\$19.0 million of impairment loss in our Asian online games and service business. Total consolidated impairment loss in 2011 was composed of a US\$2.6 million impairment loss on intangible assets for capitalized software costs and favorable lease right, a US\$247 thousand impairment loss on prepaid licensing and royalty fees, and a US\$5.1 million impairment loss on goodwill related to IAHGAMES. The total consolidated impairment loss in 2010 was composed of a US\$1.3 million impairment loss on intangible assets for capitalized software costs, a US\$870 thousand impairment loss on prepaid licensing and royalty fees, a US\$278 thousand impairment loss on fixed assets, a US\$2.3 million impairment loss on goodwill related to IAHGAMES, and a US\$22.2 million impairment loss as a result of the deconsolidation of T2CN.

**OPERATING LOSS.** Operating loss for 2011 was US\$19.9 million as compared to a loss of US\$47.7 million in 2010. The decrease in loss was primarily due to a US\$22.2 million impairment loss on deconsolidation of T2CN.

**NON-OPERATING INCOME (EXPENSES).** Non-operating loss was US\$47.7 million in 2011 compared to non-operating income of approximately US\$56.4 million in 2010. The non-operating loss in 2011 primarily included (1) US\$47.9 million loss on equity method investments, (2) US\$13.3 million impairment loss on marketable securities and investments, (3) US\$6.3 million gain on the sales of marketable securities, (4) US\$4.7 million gain on the sale of ownership interest in T2CN, and (5) US\$2.0 million gain on recovery of loss on termination of IAHGAMES' initiatives with Blizzard. The non-operating income in 2010 primarily included (1) US\$79.1 million gain on the sale of 60 percent ownership interest in our gaming software and service business, (2) US\$20.8 million loss on equity method investments, (3) US\$4.7 million impairment loss on marketable securities and investments, and (4) US\$2.6 million gain on fair value changes of warrant derivative.

**LOSS FROM DISCONTINUED OPERATIONS.** Loss from discontinued operations increased by approximately US\$4.1 million to approximately US\$4.2 million in 2011 compared to a loss of approximately US\$128 thousand in 2010, primarily due to our decision to discontinue JIDI and Shanghai JIDI and hence their operations are reported as discontinued operations for all periods presented.

**NET INCOME (LOSS) ATTRIBUTABLE TO GIGAMEDIA.** Net loss attributable to us for 2011 was approximately US\$71.2 million compared to a gain of approximately US\$2.7 million in 2010 for the reasons mentioned above.



**Table of Contents*****Business Segment Results******Asian Online Game and Service Business***

Upon our investment in IAHGames in July 2010, we held an approximate 80 percent of the controlling financial interest in IAHGames as of December 31, 2011 and consolidated IAHGames' financial results in our consolidated financial statements from July 1, 2010 through August 2012. After our divestiture in IAHGames in July 2012, we hold an approximate 20 percent of the financial interest in IAHGames and ceased consolidating IAHGames' financial results in our consolidated financial statements from August 2012 onwards. See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Acquisition and Divestiture of IAHGames .

From July 2010, due to the dispute with T2CN's former Chief Executive Officer, we were prevented from obtaining its financial information and we effectively lost control over its financial reporting process, therefore we deconsolidated its financial results from our consolidated financial statements from July 1, 2010 onwards. See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Deconsolidation of T2CN .

In addition, the financial results of our Asian online game and service business in 2011 were affected by several factors, including but not limited to strong competition from an increase of online games offered on social network platforms.

**OPERATING REVENUES.** Total operating revenues decreased by approximately US\$4.5 million, or 11.5 percent, to approximately US\$34.4 million in 2011 from approximately US\$38.9 million in 2010. Such decrease was due to (1) approximately US\$9.9 million or 100 percent decrease related to T2CN in China, which was deconsolidated from July 2010, partially offset by (2) approximately US\$2.9 million or 12.5 percent increase related to FunTown operations in Taiwan and Hong Kong, mainly due to successful launch of certain online games, and (3) approximately US\$2.5 million or 42.6 percent increase related to IAHGames operations in Southeast Asia, which was consolidated from July 2010 and contributed a full-year of revenues in 2011.

In 2011, FunTown's operation improved moderately. In spite of a decrease of 14.0 percent in the number of peak concurrent users, compared to 2010, to approximately 33,000, the number of average monthly active paying accounts was about 75,000, representing an increase of 4.8 percent compared to 2010. The average revenue per paying user ( ARPU ) was approximately US\$27.01, representing a year-over-year increase of 0.6 percent. The increase in active paying accounts and increase in ARPU resulted in an increase in revenue of 4.9 percent in local currencies or a 12.5 percent increase in revenue if translated into US dollars. As of March 31, 2012, FunTown's number of registered users was approximately 19.3 million, representing an increase of 12.2 percent compared with 2010.

**OPERATING COSTS.** Costs of our Asian online game and service revenue decreased by 15.7 percent to approximately US\$14.4 million in 2011 from US\$17.1 million in 2010. The decrease was primarily due to a decrease of approximately US\$4.4 million related to T2CN, which was deconsolidated from July 2010, partially offset by an approximately US\$1.6 million or 26.2 percent increase related to FunTown operations.

**GROSS PROFIT.** Gross profit decreased by 8.3 percent to approximately US\$20.0 million in 2011 from US\$21.8 million in 2010. Gross profit margin was approximately 58.1 percent in 2011 compared with 56.0 percent in 2010.

**OPERATING EXPENSES.** Total operating expenses decreased by approximately US\$22.7 million to approximately US\$30.9 million in 2011 from approximately US\$53.6 million in 2010. The decrease was primarily due to impairment losses related to T2CN being recorded in 2010.

**Selling and marketing expenses.** Selling and marketing expenses increased by approximately US\$1.1 million to US\$10.0 million in 2011 from US\$9.0 million in 2010. The increase was mainly due to increase in promotion activities for new games launched in FunTown operations and the inclusion of full-year expenditures in IAHGames in 2011 compared to that of the six-month period since its consolidation in July 2010.

**General and administrative expenses.** General and administrative expenses incurred in 2011 decreased by approximately US\$0.8 million to US\$9.8 million from US\$10.6 million in 2010. The decrease is mainly due to expenditure reduction in FunTown, partially offset by the inclusion of full-year expenditures in IAHGames in 2011 compared to that of the six-month period since its consolidation in July 2010.

**Impairment loss.** Impairment loss decreased by approximately US\$19.0 million to approximately US\$7.9 million in 2011 from US\$27.0 million in 2010. The impairment loss in 2011 was comprised of a US\$2.6 million impairment loss on intangible assets for capitalized software costs and favorable lease right, a US\$247 thousand impairment loss on prepaid licensing and royalty fees, and a US\$5.1 million impairment loss on goodwill related to IAHGames. The impairment loss in 2010 was comprised of a US\$1.3 million impairment loss on intangible assets for capitalized software costs, a US\$870 thousand impairment loss on prepaid licensing and royalty fees, a US\$278 thousand impairment loss on

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fixed assets, a US\$2.3 million impairment loss on goodwill related to IAHGames, and a US\$22.2 million impairment loss on deconsolidation of T2CN.

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**OPERATING LOSS.** Operating loss in 2011 was US\$10.9 million as compared to a loss of US\$31.6 million in 2010. The decrease was due to the aforementioned factors. Operating loss does not reflect certain corporate headquarter expenses.

**NON-OPERATING INCOME (EXPENSES).** Non-operating income in 2011 was US\$1.9 million compared to a loss of US\$13.2 million in 2010. The non-operating income in 2011 mainly included a gain on sales of marketable securities of US\$5.8 million, a gain of US\$4.7 million on disposal of ownership interest of T2CN, a gain of US\$1.8 million on equity method investments in relation to IAHGames, an impairment loss of US\$13.3 million on marketable securities and investments and a gain of US\$2.0 million on recovery of loss on termination of IAHGames initiatives with Blizzard. The non-operating loss in 2010 mainly included a loss of US\$12.6 million on equity method investments in relation to IAHGames online game initiatives with Blizzard, an impairment loss of US\$4.7 million on marketable securities and investments and a gain of US\$2.6 million on fair value changes of warrant derivative issued in connection with IAHGames initiatives with Blizzard.

*Gaming Software and Service Business*

On April 8, 2010, we completed the sale of a 60 percent interest in our online gaming software and service business to BetClic. From then on, we ceased to consolidate the financial results of the gaming software and service business. Our remaining non-controlling interest in Everest Gaming was accounted under the equity method until July 2012 when we entered into another agreement with BetClic to sell our remaining ownership interest in Everest Gaming. See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Divestiture of Gaming Software and Service Business .

Financial results of Everest Gaming in 2011 were negatively affected by several factors. First, the new ARJEL regulations require player liability to be fully reserved for in separate, fully-funded bank accounts by game operators, which resulted in an immediate and additional operational cash needs. Second, market conditions in France have been unfavorable, with high taxes and limitations on international play pressuring margins and lowering the appeal of online poker. Third, several European countries have introduced licensing regimes for online gaming which increased Everest Gaming's expense for online game license applications in those countries. As a result, we recorded US\$49.7 million equity loss for the remaining 40 percent interest for the year ended December 31, 2011.

**OPERATING REVENUES.** As a result of divestiture of our gaming software and service business, total operating revenues in 2011 decreased to nil in 2011 from US\$25.8 million in 2010.

**OPERATING COSTS.** As a result of divestiture of our gaming software and service business, costs of our gaming software and service revenues decreased to nil in 2011 from US\$4.0 million in 2010.

**GROSS PROFIT.** As a result of divestiture of our gaming software and service business, gross profit decreased to nil in 2011 from US\$21.8 million in 2010.

**OPERATING EXPENSES.** As a result of divestiture of our gaming software and service business, total operating expenses decreased by approximately US\$21.5 million or 99.1 percent to approximately US\$204 thousand in 2011 from approximately US\$21.7 million in 2010.

**Selling and marketing expenses.** As a result of our divestiture of our gaming software and service business, selling and marketing expenses decreased to nil in 2011 from US\$12.3 million in 2010.

**General and administrative expenses.** As a result of divestiture of our gaming software and service business, general and administrative expenses decreased by approximately US\$6.0 million to US\$204 thousand in 2011 from US\$6.2 million in 2010.

**Product development and engineering expenses.** As a result of divestiture of our gaming software and service business, product development and engineering expenses decreased to nil in 2011 from US\$3.2 million in 2010.

**OPERATING INCOME (LOSS).** The divestiture of our gaming software and service business resulted in an operating loss of US\$204 thousand in 2011 compared with an operating income of US\$78 thousand in 2010.

**NON-OPERATING INCOME (EXPENSES).** Non-operating loss increased by approximately US\$119.3 million to approximately US\$49.8 million from a non-operating income of US\$69.6 million in 2010. This deterioration is primarily because we recorded US\$49.7 million equity loss for the remaining 40 percent interest for the year ended December 31, 2011, while recognized US\$79.1 million gain from the sale of 60 percent interest in our gaming software and service business, which was partially offset by equity loss of US\$9.8 million for the remaining 40 percent interest for the period from April to December, 2010.

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For a reconciliation of business segment results to our consolidated net income attributable to us, see note 28 to our consolidated financial statements.

**Table of Contents****B. Liquidity and Capital Resources**

Our principal sources of liquidity consist of cash generated from our operations, proceeds generated from the disposal of our 60 percent shareholding in our gaming software and service business as well as marketable security investments and other assets, bank borrowings, and interest derived from our investments. Our cash and cash equivalents are held primarily in U.S. dollars, RMB and NT dollars. Our policy with respect to liquidity management is to maintain sufficient cash and cash equivalents to fund operations and strategic transactions, while placing remaining funds in higher yield investment instruments.

Our future cash requirements will depend on a number of factors including:

the rate at which we enter into strategic transactions;

the rate at which we expand our operations and employee base;

the timing of entry into new markets and new services offered;

changes in revenues and cost splits with our business partners;

the rate at which we invest in developing and licensing our products and upgrading and maintaining our network and future technologies; and

the rate at which we grow and monetize our customer bases.

As a result of our operating, investing and financing activities during 2012, the amount of our cash and cash equivalents decreased from approximately US\$64.0 million as of December 31, 2011 to US\$62.7 million as of December 31, 2012. Such decrease was primarily attributable to cash used in operating activities and for repayment of short-term borrowings, which was partially offset by investing cash inflows, which mainly consisted of proceeds from the disposal of businesses and part of our holdings in marketable securities.

The following table set forth the summary of our cash flows for the periods indicated:

| (in US\$ thousands)                                  | For the Year Ended December, 31 |             |            |
|--|---------------------------------|-------------|------------|
|  | 2010                            | 2011        | 2012       |
| Net cash used in operating activities                | \$ (8,922)                      | \$ (12,448) | \$ (7,323) |
| Net cash provided by investing activities            | 50,022                          | 11,551      | 11,117     |
| Net cash used in financing activities                | (12,364)                        | (6,225)     | (4,348)    |
| Exchange difference                                  | (410)                           | 130         | (712)      |
| Deconsolidation of T2CN                              | (12,903)                        |             |            |
| Net increase (decrease) in cash and cash equivalents | 15,423                          | (6,992)     | (1,266)    |
| Cash and cash equivalents at beginning of year       | 55,566                          | 70,989      | 63,997     |
| Cash and cash equivalents at end of year             | \$ 70,989                       | \$ 63,997   | \$ 62,731  |

OPERATING ACTIVITIES. In 2012, our net cash used in operating activities amounted to approximately US\$7.3 million, which was primarily due to loss generated from the operations of our business, and turnaround and development of our cloud computing business. In 2011, our net

cash used in operating activities amounted to approximately US\$12.4 million, which was primarily due to loss generated from the operations of our Asian online game and service business and payment of compensation previously accrued. In 2010, our net cash used in operating activities amounted to approximately US\$8.9 million, primarily due to loss generated from the operations of our Asian online game and service business.

INVESTING ACTIVITIES. Our net cash provided by investing activities in 2012 was approximately US\$11.1 million. This was primarily due to proceeds from the disposal of businesses and part of our holdings in marketable securities, totaling approximately US\$10.3 million, net of transaction costs, as well as the release of approximately US\$3.7 million from restricted cash. The cash inflows in 2012 were partially offset by capital expenditures of approximately US\$2.1 million. Our net cash provided by investing activities amounted to approximately US\$11.6 million in 2011. This was primarily due to proceeds from the disposal of T2CN and part of our holdings in marketable securities, totaling approximately US\$14.6 million, net of transaction costs, as well as the release of US\$2.0 million from restricted cash, and cash dividends of US\$1.9 million received from equity method investees. The cash inflows in 2011 were partially offset by capital expenditures of approximately US\$2.0 million and investments of approximately US\$5.2 million in loan to Everest Gaming. Our net cash provided by investing activities amounted to approximately US\$50.0 million in 2010. This was primarily due to proceeds from the sale of a 60 percent interest of the gaming software and service business of approximately US\$85.7 million, net of transaction costs, which was partially offset by capital expenditures of approximately US\$6.1 million, strategic investments in East Gate and PSI of approximately US\$6.6 million, as well as the acquisition of additional preferred shares of IAHGames of approximately US\$5.8 million, net of cash acquired.



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FINANCING ACTIVITIES. Our net cash used in financing activities in 2012 was US\$4.3 million, which was due to repayment of short-term borrowings of approximately US\$4.3 million. Our net cash used in financing activities in 2011 was approximately US\$6.2 million, US\$5.8 million of which was used in our share repurchase program. Our net cash used in financing activities in 2010 was approximately US\$12.4 million, which was primarily repayment of approximately US\$12.5 million of short-term borrowings.

As we had effectively lost control over T2CN as a result of a dispute with its former Chief Executive Officer, we deconsolidated T2CN starting from July 1, 2010; therefore, our cash and cash equivalents decreased by approximately US\$12.9 million during 2010.

We believe that our existing cash, cash equivalents, marketable securities and expected cash flow from operations will be sufficient to meet our capital expenditure, working capital, and cash obligations under our existing lease arrangements and license and other present requirements through 2013. We are seeking to dispose of certain of our investments made in certain game studios in Asia in 2013. The planned disposals are intended to free up approximately US\$15 million to US\$20 million for investment in new strategic growth initiatives, in line with our turnaround plans.

We continue to seek and review potential merger and acquisition opportunities on an ongoing basis, which may be funded through cash on our balance sheet, proceeds from sales of investments, bank borrowings or equity offerings. We do not believe that any potential merger or acquisition that we may be engaged in would alter our goal of preserving sufficient cash and cash equivalents to fund future operations.

## **Capital Expenditures**

We typically finance our capital expenditures through cash holdings. Our gross capital expenditures for equipment, furniture and fixtures, software, intangible assets and other deferred assets were US\$6.1 million, US\$2.0 million and US\$2.1 million for 2010, 2011, and 2012 respectively. Capital expenditures during 2012 were primarily for capitalized software development and computer hardware equipment for our Asian online game and service business. Our capital expenditure plans for 2013 will continue to focus primarily on software development and computer hardware equipment for our Asian online game and service business. We may adjust the amount of our capital expenditures upward or downward based on cash flow from operations, the progress of our expansion plans, and market conditions.

## **Indebtedness**

As of December 31, 2011 and 2012, short-term borrowings totaled US\$11.8 million and US\$7.7 million, respectively. These amounts were borrowed from certain financial institutions. The annual interest rates on these borrowings ranged from 1.30 percent to 7.54 percent for 2011, and 1.420 percent for 2012. The maturity dates fell in late January 2012 as of December 31, 2011, and fell in mid-January 2013 as of December 31, 2012. As of December 31, 2011 and 2012, the weighted-average interest rate on total short-term borrowings was 2.870 percent and 1.420 percent, respectively.

As of December 31, 2012, the total amount of unused lines of credit available for borrowing under these agreements was approximately US\$6.9 million.

During the period from January 2013 to March 2013, we repaid certain short-term borrowings totaling US\$22.9 million, and renewed short-term borrowing agreements totaling US\$22.9 million.

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We pledged certain time deposits, land, and buildings as collateral for borrowings from certain financial institutions. The total value of collateral amounted to US\$4.2 million and US\$0 as of December 31, 2011 and 2012, respectively, in which time deposits pledged are recorded as restricted cash totaling US\$3 million and US\$0 as of December 31, 2011 and 2012, respectively.

### **Dividends From Our Subsidiaries**

Under Singapore tax regulations, foreign-sourced dividend income used for capital expenditures, including investments, and repayment of borrowings, is not deemed as remitted to Singapore and is therefore not taxable.

In accordance with R.O.C. law, an appropriation for legal reserve amounting to 10 percent of a company's net profit is required until the reserve equals the aggregate par value of such Taiwan company's issued capital stock. As of December 31, 2011 and 2012, the legal reserves of Hoshin GigaMedia, which represent a component of our consolidated accumulated deficit, were US\$3.0 million for each period. The reserve can only be used to offset a deficit or be distributed as a stock dividend of up to 50 percent of the reserve balance when the reserve balance has reached 50 percent of the aggregate paid-in capital of Hoshin GigaMedia.

Under PRC laws and regulations, there are certain foreign exchange restrictions on our Company's PRC subsidiaries and VIE subsidiary with respect to transferring certain of their net assets to our Company either in the form of dividends, loans or advances.

As of December 31, 2012, our Company's total restricted net assets, which include paid up capital of PRC subsidiaries and the net assets of the VIE subsidiary in which our Company has no legal ownership, were approximately US\$1.5 million.

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

We make investments in research and development to keep pace and remain competitive with technology advancements and product development relating to our gaming software and service business, our Asian online game business and our new cloud computing business. For the years 2010, 2011 and 2012, we incurred US\$7.3 million, US\$2.0 million and US\$1.5 million, respectively, on research and development activities.

### **D. Trend Information**

In online games, the entire global business landscape is changing. Driven by the popularity of mobile phones and tablets and social networks, games are rapidly moving from PC-based formats to Web and mobile platforms. This in turn is causing changes in game content, as casual Web and mobile games require light content. In our market, Taiwan, the strongest demand is for casual browser/mobile games. Revenues clearly show this trend. Revenues for publishers of licensed PC-based games in Taiwan were basically flat in 2012 and profits declined. In contrast, revenues for companies focused on browser games grew at healthy double-digit rates.

We are now in the process of extending GigaMedia's PC-based online games platform to Web-based/mobile light games. This will help us capitalize on the strong growth trends of Web-based/mobile games, particularly in Asia, and our expertise in casual or light games. We have a strong offering of casual games including Asian card-based games and MahJong and a good track record of developing and monetizing them, especially in the types of games that are most popular—casino games, such as poker, slots and MahJong. We are now leveraging that expertise to transition our game portfolio from client-based games designed for PC usage to Web-based games for social networks and mobile play.

In cloud computing, the convergence of cloud, social and mobile technologies is transforming how IT services are delivered to consumers and revolutionizing how companies connect internally and externally. Cloud solutions enable firms to either avoid deployment of a full-scale onsite IT infrastructure or replace an existing company's internal IT infrastructure with an externally managed and hosted IT function. This is what is sometimes called "virtualization" of businesses. It is particularly helpful for SMEs as it brings many business benefits, including going to market faster and easier with lower capex costs.

In North America and Europe, a growing number of companies like RingCentral and 8x8 Inc have built successful businesses providing cloud computing services for SMEs. They have demonstrated that services such as hosted VoIP and cloud faxing reduce costs, increase flexibility, and drive SME productivity. However, in Taiwan and Asia, cloud services for SMEs is a largely untapped opportunity and lag the US in adoption. There are over one million SMEs in Taiwan and strong growth of cloud services regionally is forecast, driven by SMEs. The market for one segment of cloud services—business VoIP—in Asia is expected to grow at a 17% CAGR over the next five years, according to research by Global Industry Analysts, Inc. in 2013.

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In Greater China, SMEs often have no dedicated IT staff, cannot afford investment in IT systems, still rely on legacy phone and paper-based fax systems, and work outside the office. They need affordable, efficient and mobile services to conduct business in and out of the office. These customer needs point to opportunities for integrated cloud services such as those provided by GigaCloud.

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Our GigaCloud team has deep and wide knowledge in the SME market in Taiwan. We have developed an initial suite of cloud services to address the most critical needs of SMEs, including telephone, fax and storage services, which are all accessible anywhere, anytime on any smart device. We launched service in early April 2013 with tiered service offerings and special rates.

GigaCloud is an integrated platform of cloud services. Our software powers the front end and we integrate the backend solutions of our strategic technology partners.

Please see Item 3, Key Information D. Risk Factors and Item 5, Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011, and 2012 for a discussion of the most recent trends in our operating costs and revenues since the end of 2012. In addition, please refer to discussions included in this Item for a discussion of known trends, uncertainties, demands, commitments or events that we believe are reasonable likely to have a material effect on our net operating revenues, income from continuing operations, profitability or capital resources, or that would cause reported financial information not necessarily to be indicative of future operating results or financial condition.

**E. Off-Balance Sheet Arrangements**

Other than as disclosed in note 27 to our consolidated financial statements, we currently do not have (a) any obligation under a guarantee contract that has any of the characteristics identified by the FASB Accounting Standards Codification; (b) a retained or contingent interest in assets transferred to an unconsolidated entity or similar arrangement that serves as credit, liquidity or market risk support to such entity for such assets; (c) any obligation under a derivative instrument that is both indexed to our Company's own stock and classified in equity, or not reflected, in our Company's statement of financial position; or (d) any obligation, including a contingent obligation, arising out of a variable interest in an unconsolidated entity that is held by, and material to, our Company, where such entity provides financing, liquidity, market risk or credit risk support to, or engages in leasing, hedging or research and development services with, our Company.

**F. Tabular Disclosure of Contractual Obligations**

|   | As of December 31, 2012                  |              |              |             | Total |
|---|--|--------------|--------------|-------------|-------|
|   | Payment Due by Period (in US\$ thousand) |              |              |             |       |
|   | Within<br>1 year                         | 1-3<br>years | 3-5<br>years | >5<br>years |       |
| 1. Operating leases                     | 930                                      | 1,479        | 114          |             | 2,523 |
| 2. License fees*                        | 189                                      |              |              |             | 189   |
| 3. Minimum guarantees against royalties | 100                                      | 1,500        |              |             | 1,600 |
| Total contractual cash obligations      | 1,219                                    | 2,979        | 114          |             | 4,312 |

\* According to our license contracts, the total license fee payable, assuming all milestones or conditions under such license contracts were met, is approximately US\$5.7 million. Considering game performance, industry environment and business situation, management determined that certain license fees will unlikely become payable and such amount have not been included in the above table.

The initial minimum guarantees against future royalties and license fees are not required to be paid until the licensed games are commercially released or until certain milestones are achieved, as stipulated in the individual license agreements. The remaining minimum guarantees are generally required to be paid within three years subsequent to the commercial release dates of the licensed games.

**G. Safe Harbor**

See Disclosure Regarding Forward-Looking Statements on page 4 of this annual report.

**Table of Contents****ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES****A. Directors and Senior Management**

The following table sets forth information with respect to our directors and executive officers as of the date of this annual report:

| <b>Name</b>             | <b>Age</b> | <b>Position</b>  | <b>Year Appointed to Current Position</b> |
|-------------------------|------------|--|---|
| CHIEN, Mo Na            | 69         | Chairman of the Board and Executive Director   | 2012*/2012                                |
| HUANG, John Ping Chang  | 61         | Chairman of the Compensation Committee of the Board and Independent Non-Executive Director | 2012 **/2011                              |
| LIU, Nick Chia-En       | 51         | Independent Non-Executive Director   | 2011 ***                                  |
| HU ZEE, Nancy Jing-Ying | 54         | Independent Non-Executive Director   | 2003/2011****                             |
| LEE, Howe Yong          | 57         | Independent Non-Executive Director   | 2004                                      |
| TUNG, Casey Kuo Chong   | 62         | Chairman of the Audit Committee of the Board and Independent Non-Executive Director        | 2012*****/2011                            |
| HWANG, Collin           | 39         | Chief Executive Officer and Director   | 2012*****                                 |
| CHEN, Dirk Chi-Ching    | 55         | Chief Financial Officer and Director   | 2012*****/2011                            |
| HUANG, Billy Bing-Yuan  | 54         | Independent Non-Executive Director   | 2013*****                                 |

\* Mr. Mo Na CHIEN was appointed as Independent Non-Executive Director on August 2, 2010 and Executive Director on December 1, 2012. He was also appointed as Chairman of the Compensation Committee on March 15, 2011. Mr. Chien resigned as Chairman of the Compensation Committee on November 26, 2012 and was appointed as Chairman of the Board on November 5, 2012 following the resignation of Mr. Michael Y.J. DING, the former Chairman of the Board, on the same day.

\*\* Mr. John Ping Chang HUANG was appointed as Independent Non-Executive Director of the Board on January 31, 2011. He was also appointed as Chairman of the Compensation Committee on November 26, 2012.

\*\*\* Mr. Nick Chia-En LIU was appointed as Independent Non-Executive Director of the Board on March 15, 2011. He was also appointed as a member of Audit Committee on March 15, 2011.

\*\*\*\* Ms. Nancy Jing-Ying HU ZEE was appointed as Independent Non-Executive Director of the Board on July 30, 2003 and a member of Audit Committee and Compensation Committee on March 15, 2011. She resigned as a member of Audit Committee on November 15, 2011.

\*\*\*\*\* Mr. Casey Kuo Chong TUNG was appointed as Independent Non-Executive Director of the Board on November 24, 2011, and Chairman of the Audit Committee on November 5, 2012. He was also appointed as a member of the Compensation Committee on March 18, 2013.

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- \*\*\*\*\* Mr. Collin HWANG was appointed as Chief Executive Officer of our Company following the resignation of Mr. John R. STRINGER, the former Chief Executive Officer, on November 22, 2012. Mr. Hwang was appointed as Director of the Board on November 9, 2012.
- \*\*\*\*\* Mr. Dirk Chi-Ching CHEN was appointed as Chief Financial Officer of our company following the resignation of Mr. Quincy TANG, the former Chief Financial Officer, on February 1, 2012. He was appointed as Director of the Board on November 24, 2011.
- \*\*\*\*\* Mr. Billy Bing-Yuan HUANG was appointed as Independent Non-Executive Director of the Board and a member of Audit Committee on April 18, 2013.

Biographical information with respect to each of our directors and executive officers is set forth below.

### **Directors**

MO NA CHIEN is the Executive Chairman of the board of directors of our Company. He is currently the chairman of the board of S.K. Machinery Co., Ltd., as well as supervisor of the board of the Taiwan Stock Exchange-listed microelectronics firm Maxtek Technology Co., Ltd, and director of the board of Chailease Holding Company Limited and Lian Hua Foods Corporation. Mr. Chien completed the senior executive program of MIT Sloan School of Management and holds a Bachelor of Arts degree from National Taiwan University.

JOHN PING CHANG HUANG is an independent non-executive director of our Company. He is also currently the chairman of Taiwan-based Grand Pacific Investment & Development Co., Ltd., as well as the firms Chailease Construction & Development Corp., Global Hospitality Group Inc., and Beijing He Qiao Property Management Co., Ltd. Mr. Huang holds a Bachelor of Arts degree from Soochow University in Taiwan. Mr. Huang is the elder brother of Mr. Billy Bing-Yuan Huang.

NICK CHIA-EN LIU is an independent non-executive director of our Company. He was the managing director in Taiwan for a U.S. based game development company. Mr. Liu holds an MBA degree from the Stern School of Business at NYU and a bachelor's degree from the University of Southern California.

NANCY JING-YING HU ZEE is an independent non-executive director of our Company. Ms. Hu is currently a director of NHL CPA Ltd. and serves as an independent director for Enterprise Development Holdings Limited, Evendata Holding Company Limited and Arich Enterprise Co., Ltd. Ms. Hu holds a bachelor's degree from National Taiwan University, a master's degree in computers from Barry University and a Master of Business Administration degree from Florida International University.

HOWE YONG LEE is an independent non-executive director of our Company. He is currently the managing director of Lee Kim Yew (Pte) Ltd., an investment company based in Singapore, and also serves as a director of the Taiwan Stock Exchange listed, China Development Financial Holding Corporation. Mr. Lee received a Bachelor of Arts degree in business administration from the University of Washington in 1984.

CASEY KUO CHONG TUNG is an independent non-executive director of our Company. Mr. Tung is the principal owner of the accounting offices of Casey Tung in California. Mr. Tung founded the business in 1991, which serves a number of publicly listed companies in Taiwan and in China and practices in the areas of assurance, taxation, and advisory on matters such as mergers and acquisitions, financing, and reorganizations. Mr. Tung is a member of the American Institute of Certified Public Accountants and the California Society of Certified Public Accountants. He holds a Master of Science in Business Administration from California State University, Long Beach and a Bachelor of Commerce degree from Soochow University in Taiwan.

COLLIN HWANG is the CEO and a director of our Company. He currently serves as chairman of Datadot Technology Asia & Taiwan, a joint venture in Shanghai and Taipei with Australian-listed Datadot Technology Limited, a world-leading provider of identification technologies. He is also chairman of Taipei-based Cita Investment and Technology Development Co. Ltd., which invests in real estate, equities and business ventures across Asia, and chairman of Cita Aircargo Service Co. Ltd. in Taipei, one of the largest perishables logistics providers in SE Asia, where he began his career in 2000. Mr. Hwang holds a Master of Transport Management degree from the University of Sydney and a Bachelor of Construction Management degree from the University of New South Wales, Australia.

DIRK CHI-CHING CHEN is the CFO and a director of our Company. He has extensive financial leadership experience in international business and an excellent record of delivering corporate growth and strong financial performance. During a 30-year career with Chailease Finance Co., Ltd., a leading financial firm based in Taiwan with business operation in the Greater China, South East Asia, and North America, Dirk served the company in different key roles, including senior advisor, president and chief financial officer, and successfully led several important initiatives. He spearheaded growth in China, tripling the firm's revenues in that market from 2005 to 2008. Following the 2008 financial crisis, he directed a turnaround team at the firm's New York operations in 2009, developing solutions that contributed to significant improvements in financial performance. Dirk currently also serves as a non-executive director for Chailease Holdings Co., Ltd. and Chailease Finance Co. Ltd.



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BILLY BING-YUAN HUANG is an independent non-executive director of GigaMedia. He has over 20 years of experience as an executive in the technology/media industry and a proven track record of driving growth. At The Walt Disney Company, where he serves as vice president responsible for the China, Hong Kong and Taiwan markets, he launched Disney Channel and Disney Junior Channel and expanded services to new online media. At Taiwan's Videoland Communications, where he served as vice president from 1996-1998, Mr. Huang implemented a restructuring plan that transformed the business from an old production house into a modern cable television consortium distributing content for global television brands including CNN, Cartoon Network, and Discovery Channel. Prior to that, Mr. Huang was vice president of Fantasmic International, a public relations and advertising firm in Taipei, and held numerous positions with prominent advertising firms in Taipei. Mr. Huang earned a master's degree in mass communication from Texas Tech University and has a bachelor's degree in journalism from Chinese Culture University in Taipei. Mr. Huang is the younger brother of Mr. John Ping Chang Huang.

### **B. Compensation**

#### **Compensation of Directors and Executive Officers**

For the year ended December 31, 2012, the aggregate cash compensation paid by us to our directors and executive officers was approximately US\$1.7 million. For information on total amounts set aside by our Company to provide pension and retirement benefits, see note 20 to our consolidated financial statements.

As of December 31, 2012, the total outstanding number of share options granted to our directors and officers was 1,180,000, of which 104,400 shares were vested and 1,075,600 shares were unvested. As of the same date, the total number of restricted stock units granted to our directors and officers was 10,000, of which 10,000 shares were vested. For more information on stock option plans and equity incentive plans, see E. Share Ownership below.

#### **Employment of Executive Officers**

Officers are selected by and serve at the discretion of our board of directors. No executive officer is entitled to any severance benefits upon termination of his or her employment with our Company.

### **C. Board Practices**

Our board of directors is currently comprised of nine directors, including six independent non-executive members. Each of our directors is elected by our Company's shareholders and hold office until such director's successor is elected and duly qualified, or until such director's earlier death, bankruptcy, insanity, resignation or removal. No director is entitled to any severance benefits on termination of his or her service. We have established two committees of the board of directors, including the audit committee and the compensation committee.

Our audit committee currently consists of Casey Kuo-Chong TUNG, Nick Chia-En LIU and Billy Bing-Yuan HUANG. Our audit committee will select and evaluate, on our behalf, the independent public accountants who audit our annual financial statements, and will review and approve the planned scope of our annual audit, subject to the appointment, replacement or removal from office of our independent public accountants as has been approved by our shareholders at our Annual General Meeting. In accordance with our Articles of Association and our audit committee charter, all of the members of our audit committee must be persons who qualify as independent directors under the standards set forth in NASDAQ Rules 5605(c)(2)(A)(i) and (ii) and each of them is able to read and understand fundamental financial statements.

Our compensation committee currently consists of Nancy Jing-Ying HU ZEE and John Ping Chang HUANG. Our compensation committee reviews and evaluates the compensation and performance of executive officers, our Company's general compensation plans and other employee benefit plans, and performs other duties and responsibilities pursuant to the compensation committee charter. In accordance with our compensation committee charter, all of the members of the compensation committee are qualified independent directors under the standards set forth in NASDAQ Rules 5605(c)(2)(A)(i) and (ii).

### **D. Employees**

In the years ended December 31, 2010, 2011 and 2012, our total employees were 489, 562, and 287 respectively.



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As of March 31, 2013, we had a total of 288 employees, excluding part-time and temporary personnel and consultants. Of the total 288 employees as of March 31, 2013, 35 were located at our corporate headquarters, 19 were employed for our GigaCloud services, and 234 were employed for our online games business. All 288 employees were in Asia.

**E. Share Ownership****Share Ownership of Directors and Executive Officers**

The table below sets forth information as to our directors and executive officers share ownership in our Company as of March 31, 2013:

| Person                            | Number of Common Shares | Number of Shares Issuable upon exercise of options |
|-----------------------------------|-------------------------|--|
| HWANG, Collin                     | 961,200                 | 1,000,000  |
| HU ZEE, Nancy Jing-Ying           | *                       | *  |
| LEE, Howe Yong                    | *                       | *  |
| CHIEN, Mo Na                      | 0                       | *  |
| HUANG, John Ping Chang            | 0                       | *  |
| LIU, Nick Chia-En                 | 0                       | *  |
| CHEN, Dirk Chi-Ching              | 0                       | 0  |
| TUNG, Casey Kuo Chong             | 0                       | *  |
| Directors and Officers as a group | 971,200                 | 1,180,000  |

\* Less than 1 percent

All options granted to our directors and executive officers were granted pursuant to the option plans and the equity incentive plans as described under Employee Share Option Plans and Equity Incentive Plans below.

**Employee Share Option Plans and Equity Incentive Plans****2002 Employee Share Option Plan**

At the June 2002 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2002 Employee Share Option Plan (the 2002 Plan) under which up to 3,000,000 common shares of our Company were reserved for issuance. All employees, officers, directors, advisors and consultants of our Company are eligible to participate in the 2002 Plan. The 2002 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the exercise price for the option grants, to determine which eligible individuals are to receive option grants, the time or times when options grants are to be made, the number of shares subject to grant and vesting schedule.

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In August 2004, options to purchase 3,000,000 shares of our Company's common stock were granted and vested at an exercise price of US\$0.79 pursuant to the 2002 Plan. The maximum contractual term under the 2002 Plan is approximately 10 years. Termination of employment will not affect rights of exercise under vested options.

### ***2004 Employee Share Option Plan***

At the June 2004 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2004 Employee Share Option Plan (the 2004 Plan) under which up to 7,000,000 common shares of our Company were reserved for issuance. All employees, officers, directors, advisors and consultants of our Company are eligible to participate in the 2004 Plan. The 2004 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the exercise price for the option grants, to determine which eligible individuals are to receive option grants, the time or times when options grants are to be made and the number of shares subject to grant vesting schedule.

In August 2004, options to purchase 5,462,530 shares of our Company's common stock were granted at an exercise price of US\$0.79 pursuant to the 2004 Plan. These options were subject to two vesting schedules. In accordance with the terms of the first vesting schedule, 3,863,888 options were vested and exercisable upon granting. In accordance with the terms of the second vesting schedule, 1,598,642 options were granted, of which 399,663 options were vested and exercisable upon granting. The remaining 1,198,979 options were vested at a rate of 399,661 options per year from the grant date.

In May 2005, options to purchase 100,000 shares of our Company's common stock were granted at an exercise price of US\$1.45 pursuant to the 2004 Plan. In accordance with the terms of the vesting schedule, 25,000 options were vested and exercisable upon granting. The remaining 75,000 options were vested at the rate of 25,000 options per year from the grant date.

In December 2005, options to purchase 1,805,655 shares of our Company's common stock were granted at an exercise price of US\$2.55. These options were subject to two vesting schedules. In accordance with the terms of the first vesting schedule, 1,570,655 options were vested and exercisable upon granting. In accordance with the terms of the second vesting schedule, 94,000 options were vested and exercisable in December 2007. The remaining 141,000 options were vested and exercisable in December 2008.

In May 2010, options to purchase 175,000 shares of our Company's common stock were granted at an exercise price of US\$2.47. These options will be vested annually from 2010 to 2014. In accordance with the terms of the vesting schedule, 20 percent of 175,000 options will be exercisable on or after the grant date and the remaining 80 percent of 175,000 options will be exercisable annually from the first anniversary of the grant date to the fourth anniversary of the grant date.

The maximum contractual term under the 2004 Plan is 10 years. Termination of employment will not affect exercise rights under vested options. Unvested options will be forfeited upon termination of employment.

### ***2006 Equity Incentive Plan***

At the June 2006 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2006 Equity Incentive Plan (the 2006 Plan) under which up to 1,000,000 common shares of our Company have been reserved for issuance. The 2006 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2006 Plan.

In December 2006, we granted 115,000 restricted stock units (RSUs) to our employees. These RSUs were subject to two schedules for the lapsing of restrictions on transfer. 25,000 RSUs are subject to the terms of the first lapsing schedule, under which the restrictions on transfer shall lapse with respect to the first 33 percent of the RSUs upon granting with the remaining 67 percent of the RSUs vesting over a two-year period so long as the employee is employed by or providing services to our Company. 90,000 RSUs are subject to the terms of the second lapsing schedule, under which the restrictions on transfer shall lapse with respect to approximately 33 percent of the RSUs annually over a three-year period, beginning April 1, 2007 so long as the employee is employed by or providing services to our Company.

In March 2007, we granted 49,000 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to approximately 14.29 percent of the RSUs quarterly from June 2007 to December 2008 so long as the employee is employed by or providing services to our Company.



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In August 2007, we granted 30,000 RSUs to directors of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to 25 percent of the RSUs quarterly from November 2007 to August 2008 so long as the directors are providing services to our Company. In August 2007, we also granted 126,443 RSUs to employees of our Company. These RSUs were subject to two schedules for the lapsing of restrictions on transfer. 6,443 RSUs are subject to the terms of the first lapsing schedule, under which the restrictions on transfer shall lapse with respect to approximately 33 percent of the RSUs annually over a three-year period, beginning January 1, 2008 so long as the employee is employed by or providing services to our Company. 120,000 RSUs are subject to the terms of the second lapsing schedule, under which the restrictions on transfer shall lapse with respect to 6.25 percent of the RSUs quarterly from November 2007 to August 2011 so long as the employee is employed by or providing services to our Company. Also in August 2007, options to purchase 580,000 shares of our Company's common stock were granted at an exercise price of US\$10.15. In accordance with the terms of the vesting schedule, 6.25 percent of the options are vested quarterly from November 2007 to August 2011.

In October 2007, options to purchase 50,000 shares of our Company's common stock were granted at an exercise price of US\$16.60. In accordance with the terms of the vesting schedule, 6.25 percent of the options are vested quarterly from January 2008 to October 2011.

In January 2008, options to purchase 31,987 shares of our Company's common stock were granted at an exercise price of US\$16.01. In accordance with the terms of the vesting schedule, 50 percent of the options are vested annually from January 2009 to January 2010.

In January 2008, we also granted 17,113 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to approximately 50 percent of the RSUs annually from January 2009 to January 2010 so long as the employee is employed by or providing services to our Company.

In February 2010, we granted 17,790 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to 100 percent of the RSUs on the first anniversary of the grant date so long as the employee is employed by or providing services to our Company.

In May 2010, options to purchase 100,000 shares of our Company's common stock were granted at an exercise price of US\$2.47. These options will be vested annually from 2010 to 2014. In accordance with the terms of the vesting schedule, 20 percent of 100,000 options will be exercisable on or after the grant date and the remaining 80 percent of 100,000 options will be exercisable annually from the first anniversary of the grant date to the fourth anniversary of the grant date.

In May 2011, options to purchase 60,000 shares of our Company's common stock were granted at an exercise price of US\$1.25. These options will be vested annually from 2012 to 2014. In accordance with the terms of the vesting schedule, 34 percent of 60,000 options will be exercisable on or after the first anniversary of the grant date and the remaining 66 percent of 60,000 options will be exercisable annually from the second anniversary of the grant date to the third anniversary of the grant date.

In January 2012, options to purchase 20,000 shares of our Company's common stock were granted at an exercise price of US\$0.8101. These options will be vested annually from 2013 to 2015. In accordance with the terms of the vesting schedule, 34 percent of 20,000 options will be exercisable on or after the first anniversary of the grant date and the remaining 66 percent of 20,000 options will be exercisable annually from the second anniversary of the grant date to the third anniversary of the grant date.

The maximum contractual term under the 2006 Plan is 10 years. Options will be forfeited upon termination of employment, unless the relevant award agreement extends the exercisability of the outstanding options. In the event that the employee's employment with or service to our Company is terminated prior to the lapsing of restrictions with respect to any portion of the RSUs, such portion of the RSUs shall become forfeited.

### ***2007 Equity Incentive Plan***

At the June 2007 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2007 Equity Incentive Plan (the 2007 Plan) under which up to 2,000,000 common shares of our Company have been reserved for issuance. The 2007 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2007 Plan.

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In August 2007, options to purchase 465,000 shares of our Company's common stock were granted at an exercise price of US\$10.15. These options were subject to two vesting schedules. In accordance with the terms of the first vesting schedule, 6.25 percent of the 400,000 options are vested quarterly from November 2007 to August 2011. In accordance with the terms of the second vesting schedule, 25 percent of the 65,000 options are vested annually from August 2008 to August 2011.

In December 2007, options to purchase 50,000 shares of our Company's common stock were granted at an exercise price of US\$18.17. In accordance with the terms of the vesting schedule, 6.25 percent of the options are vested quarterly from March 2008 to December 2011.

In January 2008, options to purchase 18,818 shares of our Company's common stock were granted at an exercise price of US\$16.01. In accordance with the terms of the vesting schedule, 50 percent of the options are vested annually from January 2009 to January 2010.

In March 2008, we granted 51,735 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to approximately 12.5 percent of the RSUs quarterly from April 2008 to January 2010 so long as the employee is employed by or providing services to our Company.

In September 2008, we granted 465,000 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse upon the occurrence of a Change of Control so long as the employee is employed by or providing services to our Company.

In December 2008, we granted 100,000 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to approximately 25 percent of the RSUs quarterly from December 2009 to December 2012 so long as the employee is employed by or providing services to our Company.

In December 2008, options to purchase 730,000 shares of our Company's common stock were granted at an exercise price of US\$4.24. In accordance with the terms of the vesting schedule, 25 percent of the options will be vested annually from December 2009 to December 2012.

In January 2009, we granted 100,354 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to 100 percent of the RSUs on the first anniversary of the grant date so long as the employee is employed by or providing services to our Company.

In March 2010, we granted 31,000 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to approximately 50 percent of the RSUs quarterly from March 2010 to September 2010 so long as the employee is employed by or providing services to our Company.

In April 2010, we granted 323,310 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to 20, 20, and 60 percent respectively of the RSUs from September 2011 to July 2013 so long as the employee is employed by or providing services to our Company.

In May 2010, we granted 70,000 RSUs to employees of our Company. In accordance with the terms of the lapsing schedule, the restrictions on transfer shall lapse with respect to 100 percent of the RSUs on the grant date so long as the employee is employed by or providing services to our Company.

In May 2010, options to purchase 350,000 shares of our Company's common stock were granted at an exercise price of US\$2.47. These options will be vested annually from 2010 to 2014. In accordance with the terms of the vesting schedule, 20 percent of 350,000 options will be exercisable on or after the grant date and the remaining 80 percent of 350,000 options will be exercisable annually from the first anniversary of the grant date to the fourth anniversary of the grant date.

In June 2012, options to purchase 450,000 shares of our Company's common stock were granted at an exercise price of US\$1.20. In accordance with the terms of the vesting schedule, 89 percent of 450,000 options will be exercisable upon fulfillment of conditions set by the CEO of the Company and the remaining 11 percent of the 450,000 options will be exercisable on the ending date of the third anniversary of the grant date.

The maximum contractual term under the 2007 Plan is 10 years. Options will be forfeited upon termination of employment, unless the relevant award agreement extends the exercisability of the outstanding options.

### ***2008 Equity Incentive Plan***

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At the June 2008 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2008 Equity Incentive Plan (the 2008 Plan ) under which up to 1,000,000 common shares of our Company have been reserved for issuance. The 2008 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2008 Plan.

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In December 2008, options to purchase 560,000 shares of our Company's common stock were granted at an exercise price of US\$4.24. These options were subject to two vesting schedules. In accordance with the terms of the first vesting schedule, 25 percent of 360,000 options are vested annually from December 2009 to December 2012. In accordance with the terms of the second vesting schedule, 16.7 percent of the remaining 200,000 options will be vested annually from December 2009 to December 2014.

In May 2010, options to purchase 340,000 shares of our Company's common stock were granted at an exercise price of US\$2.47. These options will be vested annually from 2010 to 2014. In accordance with the terms of the vesting schedule, 20 percent of 340,000 options will be exercisable on or after the grant date and the remaining 80 percent of 340,000 options will be exercisable annually from the first anniversary of the grant date to the fourth anniversary of the grant date.

In May 2010, options to purchase 100,000 shares of our Company's common stock were granted at an exercise price of US\$2.47. These options will be vested annually from 2010 to 2012. In accordance with the terms of the vesting schedule, 34 percent of 100,000 options will be exercisable on or after the grant date and the remaining 66 percent of 100,000 options will be exercisable annually from the first anniversary of the grant date to the second anniversary of the grant date.

The maximum contractual term under the 2008 Plan is 10 years. Options will be forfeited upon termination of employment, unless the relevant award agreement extends the exercisability of the outstanding options. All options, RSUs and other share-based awards are expected to be settled by issuing new shares.

### ***2009 Equity Incentive Plan***

At the June 2009 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2009 Equity Incentive Plan (the 2009 Plan) under which up to 1,500,000 common shares of our Company have been reserved for issuance. The 2009 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2009 Plan.

In May 2010, options to purchase 1,500,000 shares of our Company's common stock were granted at an exercise price of US\$2.47. These options will be vested annually from 2010 to 2014. In accordance with the terms of the vesting schedule, 20 percent of 1,500,000 options will be exercisable on or after the grant date and the remaining 80 percent of 1,500,000 options will be exercisable annually from the first anniversary of the grant date to the fourth anniversary of the grant date.

In November 2012, options to purchase 1,000,000 shares of our Company's common stock were granted at an exercise price of US\$0.955. In accordance with the terms of the vesting schedule, 75 percent of 1,000,000 options will be exercisable upon fulfillment of conditions set by the Compensation Committee of the Board of Directors of the Company and the remaining 25 percent of the 1,000,000 options will be exercisable on the day after the third anniversary of the grant date.

The maximum contractual term under the 2009 Plan is 10 years. Options will be forfeited upon termination of employment, unless the relevant award agreement extends the exercisability of the outstanding options. All options, RSUs and other share-based awards are expected to be settled by issuing new shares.

### ***2010 Equity Incentive Plan***

At the June 2010 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2010 Equity Incentive Plan (the 2010 Plan) under which up to 1,000,000 common shares of our Company have been reserved for issuance. The 2010 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2010 Plan.

In March 2011, options to purchase 1,000,000 shares of our Company's common stock were granted at an exercise price of US\$1.05. These options will be vested annually from 2012 to 2014. In accordance with the terms of the vesting schedule, 34 percent of 1,000,000 options will be exercisable on or after the first anniversary of the grant date and the remaining 66 percent of 1,000,000 options will be exercisable annually from the second anniversary of the grant date to the third anniversary of the grant date.

In January 2012, options to purchase 600,000 shares of our Company's common stock were granted at an exercise price of US\$0.8101. In accordance with the terms of the vesting schedule, 75 percent of 600,000 options will be exercisable upon fulfillment of conditions set by the Compensation Committee of the Board of Directors of the Company and the remaining 25 percent of the 600,000 options will be exercisable on the day after the third anniversary of the grant date.





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The maximum contractual term for the options under the 2010 Plan is 10 years. Options will be forfeited upon termination of employment, unless the relevant award agreement extends the exercisability of the outstanding options. All options, RSUs and other share-based awards are expected to be settled by issuing new shares.

**Options**

In 2010, 2011 and 2012, 200,500, 0 and 0 options were exercised, respectively, and cash received from the exercise of stock options was US\$0.2 million, US\$0 and US\$0, respectively, which resulted in no significant tax benefit realized on a consolidated basis.

The options on ordinary shares of the Company outstanding as of December 31, 2012 are as follows:

| Options outstanding |                              | Weighted average remaining contractual life | Option currently exercisable |                              |
|---------------------|------------------------------|---|------------------------------|------------------------------|
| Exercise price      | No. of Shares (in thousands) |   | Exercise price               | No. of Shares (in thousands) |
| Under \$1           | 6,211                        | 2.87 years                                  | Under \$1                    | 5,191                        |
| \$1~\$10            | 2,383                        | 6.40 years                                  | \$1~\$10                     | 1,777                        |
| \$10~\$20           | 616                          | 4.65 years                                  | \$10~\$20                    | 616                          |
|                     | 9,210                        |   |                              | 7,584                        |

The number of total outstanding options as of December 31, 2012 is 9,210,191, which includes options with exercise prices of US\$0.79, US\$0.81, US\$0.96, US\$1.05, US\$1.20, US\$1.25, US\$1.45, US\$2.47, US\$2.55, US\$4.24, US\$10.15, US\$16.01 and US\$16.6. During the financial year ended December 31, 2012, a total of 2,352,460 options granted pursuant to the 2004 Plan, the 2007 Plan, the 2008 Plan and the 2010 Plan had been forfeited. During the financial year ended December 31, 2011, a total of 1,347,500 options granted pursuant to the 2004 Plan, the 2006 Plan, and the 2007 Plan, the 2008 Plan and the 2009 Plan had been forfeited.

**Employee Share Purchase Plans**

At the June 2008 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2008 Employee Share Purchase Plan (the 2008 ESPP ) under which up to 200,000 common shares of our Company were reserved for issuance. Any person who is regularly employed by our Company or our designated subsidiaries shall be eligible to participate in the 2008 ESPP. Pursuant to the 2008 ESPP, our Company would offer the Shares to qualified employees on favorable terms. Employees are also subject to certain restrictions on the amount that may be invested to purchase the shares and to other terms and conditions of the 2008 ESPP. According to the 2008 ESPP, the plan will be administered by a committee designated by the board of directors.

At the June 2009 Annual General Meeting, the shareholders of our Company approved the GigaMedia Limited 2009 Employee Share Purchase Plan (the 2009 ESPP ) under which up to 200,000 common shares of our Company were reserved for issuance. Any person who is regularly employed by our Company or our designated subsidiaries shall be eligible to participate in the 2009 ESPP. Pursuant to the 2009 ESPP, our Company would offer the Shares to qualified employees on favorable terms. Employees are also subject to certain restrictions on the amount that may be invested to purchase the shares and to other terms and conditions of the 2009 ESPP. According to the 2009 ESPP, the plan will be administered by a committee designated by the board of directors.

At the June 2010 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2010 Employee Share Purchase Plan (the 2010 ESPP ) under which up to 200,000 common shares of our Company have been reserved for issuance. To be eligible, employees must be regularly employed by us or our designated subsidiaries. Employees are also subject to certain restrictions on the amount that may be invested to purchase the shares and to other terms and conditions of the 2010 ESPP. According to the 2010 ESPP, the plan will be administered by a committee designated by the board of directors.

As of March 31, 2013, none of the 2008 ESPP, the 2009 ESPP or the 2010 ESPP has been administered by our Company.



**Table of Contents****Outstanding Options Granted Under Our Employee Share Option Plans and Equity Incentive Plans**

The following table summarizes, as of March 31, 2013, the outstanding options granted under our employee share option plans and equity incentive plans to our directors and executive officers as a group.

| <b>Date of Grant</b> | <b>Ordinary<br/>Shares</b>        | <b>Exercise<br/>Price</b> | <b>Date of Expiration</b> |
|----------------------|-----------------------------------|---------------------------|---------------------------|
|                      | <b>Underlying<br/>Outstanding</b> |                           |                           |
|                      | <b>Options</b>                    | <b>(\$/Share)</b>         |                           |
| August 12, 2004      | 40,000                            | 0.79                      | June 29, 2014             |
| December 1, 2008     | 20,000                            | 4.24                      | June 19, 2018             |
| May 13, 2010         | 40,000                            | 2.47                      | May 13, 2020              |
| May 20, 2011         | 60,000                            | 1.25                      | May 20, 2021              |
| January 5, 2012      | 20,000                            | 0.8101                    | January 5, 2022           |
| November 26, 2012    | 1,000,000                         | 0.955                     | November 26, 2022         |
| <b>Total</b>         | <b>1,180,000</b>                  |                           |                           |

**Table of Contents****ITEM 7. MAJOR SHAREHOLDERS AND RELATED-PARTY TRANSACTIONS****A. Major Shareholders**

The following table sets forth information known to us with respect to the ownership of our shares as of April 17, 2013 by each shareholder known by us to own more than 5 percent of our shares:

| Name of Owner           | Shares Owned | Percentage<br>of<br>Shares Owned |
|-------------------------|--------------|----------------------------------|
| Best Method Limited (1) | 10,799,999   | 21.29%                           |

(1) Through Best Method Limited, a British Virgin Islands company, Andre Koo has a beneficial ownership of 10,799,999 common shares of our Company.

As of April 17, 2013, we had 50,719,976 Shares outstanding, of which 39,919,977 Shares representing approximately 78.71 percent of our total outstanding Shares were not held by our major shareholders as disclosed above. As of April 17, 2013, there were 39,519,810 Shares held by 13 record holders, including nominee holders, with a registered address in the United States

The amounts and percentages of common shares beneficially owned are reported on the basis of regulations of the SEC, governing the determination of beneficial ownership of securities. Under the rules of the SEC, a person is deemed to be a beneficial owner of a security if that person has or shares voting power, which includes the power to vote or to direct the voting of such security, or investment power, which includes the power to dispose of or to direct the disposition of such security. A person is also deemed to be a beneficial owner of any securities of which that person has a right to acquire beneficial ownership within 60 days. Under these rules, more than one person may be deemed a beneficial owner of securities as to which such person has no economic interest. None of our major shareholders have voting rights different from those of our other shareholders.

**B. Related Party Transactions**

We have engaged from time to time in various transactions with related parties.

Except for the following transactions, we were not a party to any transaction with any related party that did not arise in the ordinary course of business or that was material to us.

**Borrowings**

In 2010 and 2011, to support our current operations we had short-term indebtedness from Waterland Financial Holdings ( Waterland ), a key manager of which was one of our directors. The largest amounts of outstanding short-term indebtedness to Waterland during the years ended December 31, 2010 and 2011 were \$1.5 million and \$1.7 million, respectively. As of December 31, 2011 and 2012, we did not have any indebtedness owed to Waterland.

**Loan Receivables**

We, through IAHGames, made an equity investment in Monsoon in connection with our acquisition of IAHGames with effect from July 1, 2010. In 2010, prior to our acquisition, IAHGames loaned \$5.0 million to Monsoon to support Monsoon's current operations at an interest rate of 7 percent per annum. In addition, from September to December 2010, we loaned an additional \$5.1 million to Monsoon to support its operation at an interest rate of 7 percent per annum. The largest amount outstanding to Monsoon from July 1, 2010 through August 31, 2011, after which we began to consolidate Monsoon, was \$10.3 million. As of August 31, 2011, the balance of this loan receivable was \$3.2 million, after being reduced in connection with absorbing additional losses of Monsoon. See note 16 to our consolidated financial statements for additional information.

During 2011, our Company entered into loan agreements in an aggregate of \$5.2 million with Everest Gaming, bearing interest at 3 percent per annum. As of December 31, 2011, the balance of this loan receivable was nil after being reduced in connection with absorbing additional losses

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of Everest Gaming (as discussed in more detail in note 16 to our consolidated financial statements) and considering the financial status of Everest Gaming, from which we do not expect to collect all principal and interest. We also reversed the interest recognized previously on these loans and ceased to recognize interest income going forward.

### **Stock Option Grants and Employee Share Purchase**

See Item 6, Directors, Senior Management and Employees E. Share Ownership.

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

Not applicable.

**Table of Contents****ITEM 8. FINANCIAL INFORMATION****A. Consolidated Statements and Other Financial Information****Financial Statements**

See pages beginning on page F-1 in this annual report.

**Dividend Policy**

We have neither declared nor paid any dividends on our Shares. We anticipate that we will continue to retain any earnings for use in the operation of our business, and we do not intend to pay dividends in the foreseeable future. See Item 10, Additional Information B. Memorandum and Articles of Association Dividends in this annual report.

**B. Significant Changes**

Except as disclosed in this annual report, no significant change has occurred since the date of our consolidated financial statements.

**ITEM 9. THE OFFER AND LISTING**

Not applicable, except for A. Offer and Listing Details 4. Information Regarding the Price History of the Stock and C. Markets as disclosed below.

Our Shares have been listed and traded on the NASDAQ Stock Market since February 18, 2000.

The following table shows, for the periods indicated, the high and low closing prices for our Shares as quoted on the NASDAQ Stock Market.

| <b>Year Ending December 31</b> | <b>Common Shares</b> |            |
|--------------------------------|----------------------|------------|
|                                | <b>High</b>          | <b>Low</b> |
|                                | <b>(in US\$)</b>     |            |
| 2008                           | \$ 20.70             | \$ 2.90    |
| 2009                           | \$ 7.47              | \$ 3.04    |
| 2010                           | \$ 3.32              | \$ 1.40    |
| 2011                           | \$ 1.60              | \$ 0.80    |
| 2012                           | \$ 1.49              | \$ 0.81    |

| <b>Year Ending December 31, 2011</b> | <b>Common Shares</b> |            |
|--------------------------------------|----------------------|------------|
|                                      | <b>High</b>          | <b>Low</b> |
|                                      | <b>(in US\$)</b>     |            |
| First quarter                        | \$ 1.56              | \$ 1.03    |
| Second quarter                       | \$ 1.60              | \$ 1.11    |
| Third quarter                        | \$ 1.31              | \$ 0.80    |
| Fourth quarter                       | \$ 1.06              | \$ 0.80    |

| <b>Year Ending December 31, 2012</b> | <b>Common Shares</b> |            |
|--------------------------------------|----------------------|------------|
|                                      | <b>High</b>          | <b>Low</b> |
|                                      | <b>(in US\$)</b>     |            |
| First quarter                        | \$ 1.49              | \$ 0.81    |

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|                |         |         |
|----------------|---------|---------|
| Second quarter | \$ 1.32 | \$ 1.08 |
| Third quarter  | \$ 1.16 | \$ 1.01 |
| Fourth quarter | \$ 1.08 | \$ 0.89 |

|                               | <b>Common Shares</b> |            |
|-------------------------------|----------------------|------------|
|                               | <b>High</b>          | <b>Low</b> |
|                               | <b>(in US\$)</b>     |            |
| Quarter Ending March 31, 2013 | \$ 1.20              | \$ 0.97    |

|  | <b>Common Shares</b> |            |
|--|----------------------|------------|
|  | <b>High</b>          | <b>Low</b> |
|  | <b>(in US\$)</b>     |            |
| <b>Monthly Highs and Lows</b>            |                      |            |
| October 2012                             | \$ 1.05              | \$ 0.91    |
| November 2012                            | \$ 1.08              | \$ 0.92    |
| December 2012                            | \$ 1.02              | \$ 0.89    |
| January 2013                             | \$ 1.08              | \$ 0.97    |
| February 2013                            | \$ 1.18              | \$ 1.08    |
| March 2013                               | \$ 1.20              | \$ 1.02    |
| April 2013 (only through April 16, 2013) | \$ 1.06              | \$ 1.00    |

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**ITEM 10. ADDITIONAL INFORMATION**

**A. Share Capital**

Not applicable.

**B. Memorandum and Articles of Association**

We incorporate by reference into this annual report the description of our amended memorandum and articles of association contained in our annual report for the year ended December 31, 2007 on Form 20-F (File No. 000-30540), filed with the SEC on June 30, 2008.

As of March 31, 2013, an aggregate of 50,719,976 shares have been issued and are outstanding.

There are no limitations imposed by Singapore law or by our Articles of Association on the right of a non-resident or foreign owner to hold or vote the Shares.

**C. Material Contracts**

The following are summaries of our material contracts, other than contracts entered into in the ordinary course of business, for the two years immediately preceding the date of this annual report. However, these summaries may not contain all the information important to you. For more complete information, you should read the entire agreements, which have been included as exhibits to this annual report.

**Sale of T2CN**

***Sale and Purchase Agreement among GigaMedia China Limited, Hornfull Limited, and Hangzhou NewMargin Ventures Co. Ltd., dated December 2, 2011***

On December 2, 2011, GigaMedia China Limited, Hornfull Limited, and Hangzhou NewMargin Ventures Co. Ltd. ( Hangzhou NewMargin ) entered into an agreement whereby GigaMedia agreed to sell all of its ownership interest in T2CN to Hornfull Limited and Hangzhou NewMargin agreed to guarantee the payment and performance of Hornfull Limited under the agreement. Pursuant to the agreement, GigaMedia China Limited sold all of its 43,633,681 shares of T2CN, representing a 67.087% interest in the company, to Hornfull Limited for a cash payment of US\$4,738,588. Hornfull Limited also compensated GigaMedia China Limited US\$789,765 in cash for legal fees incurred by GigaMedia in connection with the T2CN disputes. Hornfull Limited and Hangzhou NewMargin are private companies incorporated in the British Virgin Islands and the PRC, respectively.

**Sale of IAH**

***Share Purchase Agreement among Infocomm Asia Holdings Pte. Ltd., GigaMedia Asia Pacific Limited, Management Capital International Limited, and Roland Ong Toon Wah dated July 2, 2012, and***

***Share Purchase Agreement among Infocomm Asia Holdings Pte. Ltd., GigaMedia Asia Pacific Limited, Spring Asia Limited and Roland Ong Toon Wah dated July 2, 2012***

On July 2, 2012 GigaMedia Asia, IAH, MCIL, and ROTW entered into a series of agreements whereby GigaMedia Asia agreed to sell to MCIL 1,463,930 Class A shares of IAH (representing 6.48% of the issued and outstanding shares of IAH), 1,208,881 Class B shares of IAH (representing 53.52% issued and outstanding shares), and to IAH 100% of the shares in Spring Asia Limited ( Spring Asia ) held by GigaMedia through IAH. The total purchase price was US\$3 million for the Spring Asia shares, and US\$1.00 for the IAH shares, excluding taxes. All consideration for the Spring Asia shares was to be paid in four equal installments of US\$750,000 through a nine month period. The parties also executed other ancillary agreements on the same date, including the IAH Shareholders Agreement (among MCIL, GigaMedia Asia, ROTW and IAH), Share Charge Agreement (between IAH and GigaMedia Asia), and an Escrow Agreement (among IAH, GigaMedia Asia, and Trident Trust Company (Singapore) Pte. Limited).

***Settlement Agreement among Infocomm Asia Holdings Pte. Ltd., Management Capital International Ltd., GigaMedia Asia Pacific Limited, Spring Asia Limited, and Roland Ong Toon Wah dated April 17, 2013***



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IAH, MCIL, GigaMedia Asia, Spring Asia, and ROTW entered into a Settlement Agreement, dated April 17, 2013, whereby IAH and/or ROTW agreed to pay GigaMedia Asia on or before May 2, 2013 all of the outstanding Spring Asia purchase price of US\$2.25 million plus interest of US\$8,390. In addition, MCIL will purchase all of the 451,830 IAH ordinary shares held by GigaMedia at a purchase price of US\$1 million on May 2, 2013.

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### **Sale of XL Games**

#### ***Share Purchase Agreement between GigaMedia Capital Limited ( GigaMedia Capital ) and Neowiz Corporation ( Neowiz ) dated August 8, 2012***

On August 8, 2012, GigaMedia Capital entered into a Share Purchase Agreement with Neowiz, whereby GigaMedia Capital sold to Neowiz 400,000 preferred shares of XL Games representing approximately 7.2727% of the total number of issued and outstanding shares of XL Games, at a purchase price of US\$6,889,900. GigaMedia Capital and Neowiz also executed two license agreements, one for GigaMedia Capital to license to Neowiz certain game software for a fee of US\$1.5million, and the other for Neowiz to grant GigaMedia a non-exclusive license in Taiwan, Hong Kong, Macau and Southeast Asia on certain game software free of any license fee for three years.

### **Other Material Contracts**

Other material contracts are incorporated by reference to our annual reports for the year ended December 31, 2009, for the year ended December 31, 2010 and for the year ended December 31, 2011 on Form 20-F (File No. 000-30540) and for additional information on our material contracts, see Item 7, Major Shareholders and Related Party Transactions B. Related Party Transactions in this annual report.

### **D. Exchange Controls**

Foreign investment regulations of PRC may affect our ability to retrieve our capital investments in China. Under the current PRC regulations, conversion of Renminbi is permitted in China for routine current-account foreign exchange transactions, including trade and service related foreign exchange transactions, payment of dividends and service of foreign debts. Conversion of Renminbi for most capital-account items, such as direct investments, investments in PRC securities markets and repatriation of investments, however, is still subject to the approval of the State Administration of Foreign Exchange (SAFE) or its local competent branches. Foreign-invested enterprises, such as our PRC subsidiaries, may buy, sell and/or remit foreign currencies for current-account transactions at banks in the PRC with authorization to conduct foreign exchange business by complying with certain procedural requirements, such as presentment of valid commercial documents. For capital-account transactions involving foreign direct investment, foreign debts and outbound investment in securities and derivatives, approval from SAFE or its local competent branches is a pre-condition. Capital investments by foreign-invested enterprises outside the PRC are subject to limitations and requirements in the PRC, such as prior approvals from the Ministry of Commerce, or MOFCOM, SAFE and the National Development and Reform Commission of the PRC.

### **E. Taxation**

#### **Singapore Tax Considerations**

##### ***Taxation of Dividends Received by Singapore Resident Shareholders***

On the basis that we are not tax resident in Singapore, dividends paid by us would be taxable in Singapore if they are received in Singapore or if they are considered, in the hands of a particular shareholder, to be derived in Singapore (for example if they constitute the income of a trade or business carried out in Singapore).

Foreign-sourced dividends received by a Singapore resident person on or after June 1, 2003 will be exempt from tax if certain conditions are met. The main conditions to be satisfied for such exemption are that:

the dividends are received from a jurisdiction with a maximum tax rate on the trade or business income of a company of at least 15 percent; and

the dividends themselves, or the income from which they are paid, have been subject to tax in the foreign jurisdiction or have been exempted from tax under an incentive granted for substantive business activities.

The normal tax rate for corporate profits in Singapore is 17 percent for the year of assessment 2012 and 2013 (i.e., for the income earned in the financial year or other basis period ended 2011 and 2012 respectively). Resident individuals are subject to tax at progressive rates of up to 20 percent.

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If our shareholders are corporations, our shareholders will be regarded as being tax resident in Singapore if the control and management of our shareholders' business is exercised in Singapore. For example, if the board of directors of a company meets and conducts the business of such company in Singapore, such company would generally be regarded as tax resident in Singapore. An individual will be regarded as being tax resident in Singapore in a year of assessment if, in the preceding year, he was physically present in Singapore or exercised an employment in Singapore (other than as director of a company) for 183 days or more, or if he resides in Singapore.

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All foreign-sourced income received in Singapore (except for income received through a partnership in Singapore) on or after January 1, 2004 by tax resident individuals will be exempt from tax.

### ***Gains on Disposal of Shares***

Singapore does not impose tax on capital gains. However, there are no specific laws or regulations which deal with the characterization of capital gains and hence, gains on disposal of shares may be construed to be of an income nature and subject to Singapore income tax if they arise from or are otherwise connected with the activities which the Inland Revenue Authority of Singapore regards as the carrying on of a trade or business in Singapore. You should consult your tax advisors concerning the Singapore tax consequences of acquiring, owning, selling or otherwise disposing the Shares.

### ***Stamp Duty***

There is no stamp duty payable in respect of the issuance and holding of our Shares. Where existing shares are acquired in Singapore, stamp duty is payable on the instrument of transfer of the shares at the rate of S\$2.00 for every S\$1,000 or any part thereof, of the consideration for or market value of the shares, whichever is higher. The stamp duty is borne by the purchaser unless there is an agreement to the contrary. Where an instrument is executed outside Singapore, or no instrument of transfer is executed, no stamp duty is payable on the acquisition of existing shares. However, stamp duty would be payable if an instrument of transfer which is executed outside Singapore is received in Singapore.

Under Singapore law, our directors may not register a transfer of our Shares unless the instrument of transfer has been duly stamped.

### ***Singapore Estate Duty***

Estate duty has been abolished for deaths occurring on or after February 15, 2008.

You should consult your tax advisors regarding the non-Singapore estate duty consequences of your ownership of our Shares.

### ***Goods and Services Tax ( GST )***

The sale of our Shares by an investor belonging in Singapore to another person belonging in Singapore is an exempt supply not subject to GST. Any GST directly or indirectly incurred by the investor in respect of this exempt supply would be a cost to the investor.

Where our Shares are sold by a GST-registered investor to a person belonging outside Singapore and that person is outside Singapore when the sale is executed, the sale should generally be considered as a taxable supply subject to GST at zero-rate. Any GST incurred by the investor in the making of such a supply, if the same is a supply in the course of or furtherance of a business, may be fully recoverable from the Comptroller of GST.

Services such as brokerage, handling and clearing services rendered by a GST-registered person to an investor belonging in Singapore in connection with the investor's purchase, sale or holding of our Shares will be subject to GST at the rate of 7 percent. Similar services rendered to an investor belonging outside Singapore should generally be subject to GST at zero-rate.

## **U.S. Tax Considerations**

### ***U.S. Federal Income Tax Considerations for U.S. Persons***

The following is a discussion of certain U.S. federal income tax considerations for investors in Shares that are U.S. persons (as defined below). This discussion is based on U.S. federal income tax law as in effect on the date hereof, which is subject to differing interpretations or change, possibly on a retroactive basis. This discussion applies only to U.S. persons that will acquire the Shares and will hold the Shares as capital assets (generally, property held for investment). This discussion is for general information only and does not address all of the tax considerations that may be relevant to you in light of your particular circumstances or if you are subject to special treatment under the U.S. federal income tax laws, including if you are a:

bank;

broker-dealer;

financial institution or insurance company;

tax-exempt entity;

person holding Shares as part of a straddle, hedge, conversion or other integrated investment;

a person owning, actually or constructively, 10 percent or more of the combined voting power of all classes of our stock;

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

a partnership or a partner of such partnership; or

a trader in securities that has elected the mark-to-market method of accounting for securities.

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This discussion does not address any U.S. state, local or non-United States tax considerations, or any U.S. federal estate, gift or alternative minimum tax considerations.

As used in this discussion, the term "U.S. person" means:

an individual who is a citizen or resident of the United States;

a corporation, or other entity treated as a corporation for U.S. federal income tax purposes, created in or organized under the laws of the United States or any political subdivision thereof;

an estate, the income of which is includible in gross income for U.S. federal income tax purposes regardless of its source; or

a trust if (1) it is subject to the primary supervision of a court within the United States and one or more U.S. persons have the authority to control all substantial decisions of the trust, or (2) it has otherwise elected to be treated as a U.S. person under the Internal Revenue Code.

If a partnership (including any entity treated as a partnership for U.S. federal income tax purposes) holds Shares, the tax treatment of a partner in such partnership will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding Shares, you are urged to consult your tax advisor as to the particular U.S. federal income tax consequences of an investment in the Shares that is applicable to you.

You are urged to consult your tax advisor concerning the particular U.S. federal, state, local and non-United States income and other tax considerations regarding the ownership and disposition of the Shares, including the application of the passive foreign investment company rules discussed below. Investors should carefully review the discussion below under "Passive Foreign Investment Company Rules."

***Passive Foreign Investment Company***

Due to the price of our Shares during 2012 and the composition of our assets (in particular, the retention of a large amount of cash and our significant portfolio of investment securities), we believe that it is likely that we were classified as a passive foreign investment company ("PFIC"), for United States federal income tax purposes, for the taxable year ended December 31, 2012, and we will likely be a PFIC for our current taxable year ending December 31, 2013 unless our share value increases and/or we invest a substantial amount of the cash and other passive assets we hold in assets that produce or are held for the production of non-passive income. In general, we will be classified as a PFIC for any taxable year if either (i) 75 percent or more of our gross income for such year is passive income or (ii) 50 percent or more of the average quarterly value of our assets (as generally determined on the basis of fair market value) produce or are held for the production of passive income. For this purpose, cash and assets readily convertible into cash are generally classified as passive and goodwill and other unbooked intangibles associated with active business activities may generally be classified as non-passive. We will be treated as owning a proportionate share of the assets and earning a proportionate share of the income of any other corporation in which we own, directly or indirectly, more than 25 percent (by value) of the stock.

If we are classified as a PFIC for any taxable year during which you hold Shares, and unless you make a mark-to-market election (as described below), you will generally be subject to special tax rules that have a penalizing effect, regardless of whether we remain a PFIC, on (i) any excess distribution that we make to you (which generally means any distribution received by you in a taxable year that is greater than 125 percent of the average annual distributions received by you in the three preceding taxable years or your holding period for the Shares, if shorter), and (ii) any gain realized on the sale or other disposition, including a pledge, of our Shares. Under the PFIC rules:

such excess distribution or gain will be allocated ratably over your holding period for the Shares;

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such amount allocated to the current taxable year and any taxable year prior to the first taxable year in which we are classified as a PFIC (a pre-PFIC year ) will be taxable as ordinary income;

such amount allocated to each prior taxable year, other than a pre-PFIC year, will be subject to tax at the highest tax rate in effect applicable to you for that year; and

an interest charge generally applicable to underpayments of tax will be imposed on the tax attributable to each prior taxable year, other than the current taxable year or a pre-PFIC year.

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As an alternative to the foregoing rules, a holder of marketable stock in a PFIC may make a mark-to-market election, provided that the Shares are regularly traded on a qualified exchange. Although we believe that, based on the current level of trading activity of our Shares on the NASDAQ Global Market, the Shares should qualify as being regularly traded on a qualified exchange, no assurance can be given that the Shares will continue to be readily tradable on an established securities market in the United States. If you make this election, you will generally (i) include in gross income for each taxable year the excess, if any, of the fair market value of your Shares at the end of the taxable year over the adjusted tax basis of the Shares and (ii) deduct as an ordinary loss the excess, if any, of the adjusted tax basis of the Shares over the fair market value of the Shares at the end of the taxable year, but only to the extent of the amount previously included in income as a result of the mark-to-market election. Your adjusted tax basis in the Shares would be adjusted to reflect any income or loss resulting from the mark-to-market election. If you make a mark-to-market election in respect of a corporation classified as a PFIC and such corporation ceases to be classified as a PFIC, you will generally not be required to take into account the gain or loss described above during any period that such corporation is not classified as a PFIC. If you make a mark-to-market election, any gain you recognize upon the sale or other disposition of Shares will be treated as ordinary income and any loss will be treated as ordinary loss, but such loss will only be treated as ordinary to the extent of the net amount previously included in income as a result of the mark-to-market election. In the case of a U.S. person who has held Shares during any taxable year in which we are classified as PFIC and continues to hold such Shares (or any portion thereof), and who is considering making a mark-to-market election, special tax rules may apply relating to purging the PFIC taint of such Shares. If a U.S. Holder makes a mark-to-market election, the tax rules that apply to distributions by corporations which are not PFICs would apply to distributions, except that the reduced tax rate applicable to qualified dividend income (as discussed below in Dividends) would not apply.

Because a mark-to-market election cannot be made for any lower-tier PFICs that we may own, a U.S. Holder may continue to be subject to the PFIC rules with respect to such U.S. Holder's indirect interest in any investment held by us that is treated as an equity interest in a PFIC for United States federal income tax purposes.

We do not intend to provide the U.S. persons with the information necessary to permit U.S. persons to make qualified electing fund elections, which, if available, would result in tax treatment different from (and generally less adverse than) the general tax treatment for PFICs described above.

Each U.S. person who holds a PFIC is required to file an annual report containing such information as the U.S. Treasury may require. In addition, if a U.S. person holds Shares in any year in which we are a PFIC, such holder will be required to file Internal Revenue Service Form 8621 regarding distributions received on the Shares, any gain realized on the disposition of the Shares, and any reportable election. You are urged to consult your tax advisor regarding the application of the PFIC rules, including the possibility of making a mark-to-market election.

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

Except as discussed above with respect to the passive foreign investment company tax rules, the amount of distributions you receive on your Shares (other than certain pro rata distributions of our Shares or rights to subscribe for Shares) will generally be reported as dividend income to you if the distributions are made from our current and accumulated earnings and profits as calculated according to U.S. federal income tax principles. Because we do not intend to determine our earnings and profits on the basis of U.S. federal income tax principles, any distribution paid will generally be reported as a dividend for U.S. federal income tax purposes. You will include such dividends in your gross income as ordinary income on the day you actually or constructively receive them. The amount of any distribution of property other than cash will be the fair market value of such property on the date it is distributed. A non-corporate recipient of dividend income will generally be subject to tax on dividend income from a qualified foreign corporation at a reduced United States federal tax rate rather than the marginal tax rates generally applicable to ordinary income, so long as certain holding period requirements are met. A non-U.S. corporation generally will be considered to be a qualified foreign corporation (i) if it is eligible for the benefits of a comprehensive tax treaty with the United States which the Secretary of Treasury of the United States determines is satisfactory for purposes of this provision and which includes an exchange of information program or with respect to any dividend it pays on stock which is readily tradable on an established securities market in the United States and (ii) the corporation is not a PFIC and is not treated as a PFIC with respect to you for the taxable year in which the dividend was paid and the preceding taxable year. There is currently no tax treaty in effect between the United States and Singapore. Although the Shares are currently tradable on the NASDAQ Global Market, which is an established securities market in the United States, no assurance can be given that the Shares will continue to be readily tradable on an established securities market in the United States. U.S. corporate holders will generally not be eligible for the dividends received deduction allowed to corporations.

The amount of any distribution paid in a currency other than the U.S. dollar will equal the U.S. dollar value of the foreign currency you receive, calculated by reference to the exchange rate in effect on the date you actually or constructively receive the distribution, regardless of whether the foreign currency is actually converted into U.S. dollars. If you do not convert the foreign currency you receive as a dividend on the date of receipt, you will have a basis in such foreign currency equal to its U.S. dollar value on the date of receipt. Any gain or loss you realize when you subsequently sell or otherwise dispose of such foreign currency generally will be ordinary income or loss from sources within the United States for foreign tax credit limitation purposes.





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Dividends will generally be treated as foreign source income for U.S. foreign tax credit purposes and generally will constitute passive category income. A U.S. person may be eligible, subject to a number of complex limitations, to claim a foreign tax credit in respect of any foreign withholding taxes imposed on dividends received on Shares. A U.S. person who does not elect to claim a foreign tax credit for foreign tax withheld may instead claim a deduction for U.S. federal income tax purposes, in respect of such withholding, but only for a year in which such holder elects to do so for all creditable foreign income taxes. The rules governing the foreign tax credits are complex. Accordingly, you are urged to consult your tax advisor regarding the availability of a foreign tax credit under your particular circumstances.

### ***Sale or other disposition of Shares***

Except as discussed above with respect to the passive foreign investment company tax rules, a U.S. person generally will recognize capital gain or loss for U.S. federal income tax purposes upon a sale or other disposition of our Shares in an amount equal to the difference between the amount realized from the sale or disposition and the holder's adjusted tax basis in the Shares. Such gain or loss generally will be long-term (taxable at a reduced rate for individuals) if, on the date of sale or disposition, the Shares were held by the holder for more than one year and will generally be treated as gain or loss from U.S. sources for foreign tax credit purposes. The deductibility of a capital loss may be subject to limitations. You are urged to consult your tax advisor regarding the consequences if a foreign withholding tax is imposed on a disposition of Shares, including the availability of the foreign tax credit under your particular circumstances.

### ***Backup Withholding and Information Reporting***

U.S. persons may be subject to information reporting to the Internal Revenue Service with respect to dividends on and proceeds from the sale or other disposition of our ADSs or common shares. Dividend payments with respect to our ADSs or common shares and proceeds from the sale or other disposition of our ADSs or common shares are not generally subject to United States backup withholding (provided that certain certification requirements are satisfied). You are advised to consult your tax advisor regarding the application of the United States information reporting and backup withholding rules to your particular circumstances.

Individuals who are U.S. Holders, and who hold specified foreign financial assets, including stock of a non-U.S. corporation that is not held in an account maintained by a U.S. financial institution, whose aggregate value exceeds US\$50,000 during the tax year, may be required to attach to their tax returns for the year certain specified information. An individual who fails to timely furnish the required information may be subject to a penalty. Each U.S. person who is an individual is advised to consult its tax advisor regarding its reporting obligations under this legislation.

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

Not applicable.

### **G. Statements by Experts**

Not applicable.

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

The SEC allows us to incorporate by reference the information we file with the SEC. This means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference in this annual report is considered to be part of this annual report. We therefore incorporate by reference in Item 19 of this annual report certain exhibits, which we filed with the SEC in prior filings. You may read and copy this annual report, including the exhibits incorporated by reference in this annual report, at the public reference room maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. You can request copies of these documents upon payment of a duplicating fee, by writing to the SEC. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference rooms. Additional information may also be obtained over the Internet at the SEC's website at [www.sec.gov](http://www.sec.gov).

You may also request a copy of our SEC filings, at no cost, upon written request to our investor relations department at 8th Floor, No. 22, Lane 407, Section 2, Tiding Boulevard, Taipei 11492, Taiwan R.O.C, or by e-mail to: [Brad.Miller@Gigamedia.com](mailto:Brad.Miller@Gigamedia.com). A copy of each report submitted in accordance with applicable U.S. law is also available for public review at our principal executive offices.

As a foreign private issuer, we are exempt under the Securities Exchange Act from, among other things, the rules prescribing the furnishing and content of proxy statements, and our executive officers, directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Securities Exchange Act. In addition, we will not be required under the Securities Exchange Act to file periodic reports and financial statements with the SEC as frequently or as promptly as U.S. companies whose securities are

registered under the Securities Exchange Act.

**I. Subsidiary Information**

Not applicable.

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**ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Market risk is the risk of loss related to adverse changes in market prices, including interest rates and foreign exchange rates, of financial instruments. We are exposed to various types of market risks in the normal course of business, including changes in interest rates and foreign currency exchange rates.

**Foreign Currency Risk**

Our subsidiaries conduct most of their business transactions in their own measurement currencies; therefore the foreign currency risks derived from operations are not significant. However, we hold some assets or liabilities in foreign currencies other than measurement currency and the value of these assets and liabilities are subject to foreign currency risks resulting from fluctuations in exchange rates between the foreign-denominated currency and the measurement currency. We have not used hedging transactions to reduce our exposure to exchange rate fluctuations; however, we may choose to do so in the future. For more information on foreign currency translations for our financial reporting purposes, see note 1(b) to our audited consolidated financial statements beginning on page F-1 in this annual report.

As of December 31, 2012, we had bank deposits of approximately US\$2.4 million denominated in foreign currencies other than measurement currencies of the entities holding such assets. These assets are subject to foreign currency exchange risk. We recorded a realized foreign exchange loss of approximately US\$32 thousand and unrealized foreign exchange gain of approximately US\$473 thousand in the year ended December 31, 2012.

As of December 31, 2012, we had available-for-sale marketable securities and investments of approximately US\$25.7 million which were denominated in foreign currencies other than measurement currencies of the entity holding such assets. Future fluctuation of the exchange rates could impact the periodic impairment assessment on other-than-temporary loss of these assets.

Based on the sensitivity analysis of our exposure to foreign currency exchange rate risk related our bank deposits and available-for-sale marketable securities which were denominated in a foreign currency other than functional currencies of the entities holding such assets, a hypothetical 10 percent change in the exchange rate between the U.S. dollar and the underlying currencies of those instruments subject to foreign currency exchange rate risk would result in a change of approximately 2.0 percent in our total equity as of December 31, 2012.

**Interest Rate Risk**

Our exposure to interest rates relates primarily to our short-term loans from various banks. The variations in fair value of the marketable securities that we owned as of December 31, 2012 do not have direct relationship with interest rates changes. As of December 31, 2012, we had no investment in fixed-income or money market investment funds. Declines in interest rates over time will, however, reduce our interest income from our bank deposits. Increases in interest rates of the loans will increase our interest expenses. As of December 31, 2012, we had approximately US\$7.7 million of short-term loans, with a weighted average interest rate of approximately 1.42 percent. Based on our sensitivity analysis with respect to our short-term loans, we have no significant exposure to fluctuations in interest rates. We have not entered into any interest rate swaps, caps or hedge contracts to modify our exposure to interest rate fluctuations.

We did not include a quantitative tabular disclosure regarding the foreign currency risk and the interest rate risk. As noted above, we believe that the magnitude of selected hypothetical changes to such market risks on the consolidated financial statements is not significant. However, we cannot assure you that we will not be affected by these risks in the future.

**Other Market Risks**

We are also exposed to other market risks, which are mainly derived from our investments. Changes in the stock price, performance or net asset value of the companies that we invested and investment funds might have significant impact on our financial positions or operating results.

**ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

Not applicable.

**PART II**

**ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

None.

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**ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS**

**A. Material Modification to the Instruments Defining the Rights of Security Holders**

None.

**B. Material Modification to the Rights of Registered Securities by Issuing or Modifying or any Other Class of Securities**

None.

**C. Withdrawal or Substitution of a Material Amount of the Assets Securing any Registered Securities**

Not applicable.

**D. Change of Trustees or Paying Agents for any Registered Securities**

None.

**E. Use of Proceeds**

Not applicable.

**ITEM 15. CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures**

Our management, with the participation of our chief executive officer and our chief financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined by Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of December 31, 2012. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, in designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable, rather than absolute, assurance of achieving the desired control objectives, and management was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Based upon that evaluation, and taking into account the foregoing, our chief executive officer and chief financial officer have concluded that, as of December 31, 2012, our disclosure controls and procedures were effective in providing reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act was recorded, processed, summarized and reported on a timely basis, and these controls and procedures were effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act was accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

**Management's Annual Report on Internal Control Over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined by Rules 13a-15(f) and 15d-15(f) under the Exchange Act). Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles in the United States ( US GAAP ). Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with US GAAP and that receipts and expenditures are being made only in accordance with authorizations of our management and directors and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements. Also, projections of any evaluation of the effectiveness of internal control to future periods are subject to the risk that controls may become inadequate because of

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changes in conditions, and that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2012. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control - Integrated Framework. Based on our assessment using those criteria, our management has concluded that our internal control over financial reporting as of December 31, 2012 was effective.

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**Attestation Report of the Independent Registered Public Accounting Firm**

The effectiveness of our internal control over financial reporting as of December 31, 2012 has been audited by GHP Horwath, P.C., our independent registered public accounting firm, who has also audited the consolidated financial statements included in this annual report on Form 20-F and, as part of the audit, has issued a report, which appears on pages F-1 and F-2 of this annual report, on the effectiveness of our internal control over financial reporting.

**Changes in Internal Control Over Financial Reporting**

During the year ended December 31, 2012, there were no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**ITEM 16. Reserved**

**ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

Our board of directors has determined that Mr. Casey Kuo Chong TUNG, an independent director and member of our audit committee, is the audit committee financial expert.



**Table of Contents****ITEM 16B. CODE OF ETHICS**

We have adopted a code of ethics, as defined in Item 16B of Form 20-F. Our code of ethics applies to our chief executive officer, chief financial officer and persons performing similar functions, as well as to our directors, other officers, employees and consultants. The code of ethics was amended on December 19, 2005, May 10, 2006 and February 13, 2009 in order to conform certain provisions in it with our newly adopted anti-fraud policy. The code of ethics was also amended on April 30, 2010 to incorporate non-competition and non-solicitation provisions. The full text of our code of ethics is available on our website, [www.gigamedia.com](http://www.gigamedia.com). If we further amend any provisions of our code of ethics that apply to our chief executive officer, chief financial officer or persons performing similar functions, or if we grant any waiver of such provisions, we will disclose such amendment or waiver on our website at the same address. We will also provide any person without charge a copy of our code of ethics upon written request to our investor relations department at 8 th Floor, No. 22, Lane 407, Section 2, Tiding Boulevard, Taipei 114, Taiwan R.O.C., or by e-mail to: [Brad.Miller@Gigamedia.com](mailto:Brad.Miller@Gigamedia.com).

On December 19, 2005, our board of directors adopted an anti-fraud policy for the purpose of preventing fraud schemes, including fraudulent financial reporting misappropriation of assets, any fraud committed by senior management, and information technology fraud. According to our anti-fraud policy, our audit committee is responsible for monitoring the implementation of our anti-fraud policy and procedures, and an anti-fraud taskforce is assigned by our audit committee to be responsible for the anti-fraud hotline management, risk assessment, complaint investigation and resolution, and reporting to our chief executive officer, chief financial officer and audit committee.

On May 10, 2006, our audit committee adopted a whistleblower program pursuant to our anti-fraud policy. The whistleblower program enables all employees to know how and when to use the whistleblower hotline and communicate or report, on a confidential or anonymous basis, without fear of retribution, concerns related to wrongdoings or violations, and ensures that all reported incidents are properly investigated.

On February 13, 2009, the code of ethics was amended to include the anti-fraud taskforce's reporting obligation to our chief executive officer, chief financial officer, chief operating officer and audit committee after reviewing our anti-fraud policy, guidelines on fraud risk assessment and whistleblower program annually.

On April 30, 2010, our board of directors adopted a non-competition provision under which all of our employees, consultants, officers and directors may not participate, invest, license, employ or being employed, or cooperate with any company or entity engaged in a line of business which may be competitive with the business of the Company within three months after termination of their employment of the Company, except in cases where the local law or the contract states otherwise. The Company may take legal actions against such employees, consultants, officers or directors in the event that non-competition obligations are being violated. An amended non-solicitation provision was also adopted, under which all our employees, consultants, officers and directors may not, during their employment or within twelve months after termination of the employment, directly or indirectly, solicit, entice, or attempt to approach, solicit or entice any of the other employees of the Company or its affiliates to terminate the employment.

**ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The following table summarizes the aggregate fees billed to us by GHP Horwath, P.C. for services performed relating to the fiscal years ended December 31, 2011 and 2012.

| <b>For the Years Ended December 31,</b> | <b>2011</b>      | <b>2012</b>      |
|---|------------------|------------------|
|   | <b>(in US\$)</b> | <b>(in US\$)</b> |
| Audit Fees                              | 835,898          | 702,452          |
| Audit-Related Fees                      | 0                | 8,060            |
| Tax Fees                                | 18,096           | 18,461           |
| All Other Fees                          | 0                | 0                |

**A. Audit Fees**

Audit fees consist of fees billed for the annual audit of our consolidated financial statements. Audit fees also include fees for services that are normally provided by the independent registered public accounting firm in connection with statutory and regulatory filings or engagements.

**B. Audit-Related Fees**

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Audit-related fees consist of fees billed for assurance and related services that are reasonably related to the performance of the audit or review of our consolidated financial statements, and are not reported under the paragraph captioned "Audit Fees" above. Audit related fees billed in 2012 consisted of accounting consultations in connection with business dispositions.

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**C. Tax Fees**

Tax fees include fees billed for tax compliance services, including the preparation of original and amended tax returns, and tax advisory services.

**D. All Other Fees**

All other fees are fees billed for services provided by the independent registered public accounting firm other than the services reported as audit fees, audit-related fees and tax fees above. No other fees were billed during 2011 and 2012.

**E. Audit Committee Pre-Approval Policies and Procedures**

In May 2005, we adopted our audit committee charter. Consistent with the SEC's policies regarding auditor independence, our audit committee is directly responsible for the appointment, compensation, retention and oversight of the work of auditors engaged to provide us with audit, review or attest services. Our audit committee has sole discretion to review and pre-approve the appointment of auditors and to set their fees for the performance of audit and non-prohibited non-audit services in accordance with the Sarbanes-Oxley Act of 2002 and the SEC rules and regulations promulgated thereunder, subject to the appointment, replacement or removal from office of our independent public accountants as approved by our shareholders at our Annual General Meeting.

The appointment of our independent registered public accounting firm, GHP Horwath, P.C., as well as the scope of each audit, audit-related or non-prohibited, as well as any non-audit services provided pursuant to such appointment, and our auditors' fees for all such services, were approved by our audit committee.

**ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not applicable.

**ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

See Item 5. Operating and Financial Review and Prospects A. Operating Results Certain Significant Events Affecting Our Results of Operations for 2010, 2011 and 2012 Share Repurchase Program in this annual report.

**ITEM 16F. CHANGES IN REGISTRANT'S CERTIFYING ACCOUNTANTS**

Not applicable.

**ITEM 16G. CORPORATE GOVERNANCE**

**Summary of Significant Differences in Corporate Governance Practices**

Our Shares are currently listed on the NASDAQ Stock Market and, for so long as our securities continue to be listed, we will remain subject to the rules and regulations established by NASDAQ as being applicable to listed companies. Under NASDAQ Rule 5615(a)(3), a foreign private issuer such as our Company may follow its home country practice in lieu of the requirements of the NASDAQ Rule 5600 Series, with certain exceptions, provided that it discloses each requirement that it does not follow and describes the home country practice followed in lieu of such requirements. In addition, NASDAQ has amended its Rule 5615(a)(3) to permit foreign private issuers to follow certain home country corporate governance practices without the need to seek an individual exemption from NASDAQ. However, a foreign private issuer must disclose in its annual report filed with the SEC each requirement it does not follow and the alternative home country practice it does follow.

We are incorporated under the laws of Singapore. We currently comply with the specifically mandated provisions of NASDAQ Rule 5615(a)(3). We are currently exempt from the DRS eligibility provisions of NASDAQ Rule 5255(c) as we are not allowed to issue of non-certificated securities under Singapore law. See Item 9, The Offer and Listing in this annual report. We have elected to voluntarily comply with other requirements of NASDAQ Rule 5615(a)(3) in all material aspects, notwithstanding that our home country does not mandate compliance; although we may in the future determine to cease voluntary compliance with those provisions of NASDAQ Rule 5615(a)(3).



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**ITEM 16H. MINE SAFETY DISCLOSURE**

**NOT APPLICABLE**

**PART III**

**ITEM 17. FINANCIAL STATEMENTS**

We have elected to provide financial statements pursuant to Item 18.

**ITEM 18. FINANCIAL STATEMENTS**

Our consolidated financial statements and the report thereon by our independent registered public accounting firm listed below are attached hereto as follows:

|  | <b>Page</b> |
|--|-------------|
| <u>(a) Report of Independent Registered Public Accounting Firm</u>   | F-1 F-2     |
| <u>(b) Consolidated Balance Sheets as of December 31, 2011 and 2012</u>  | F-3 F-4     |
| <u>(c) Consolidated Statements of Income (Loss) for the years ended December 31, 2010, 2011 and 2012</u>               | F-5         |
| <u>(d) Consolidated Statements of Comprehensive Income (Loss) for the years ended December 31, 2010, 2011 and 2012</u> | F-6         |
| <u>(e) Consolidated Statements of Equity for the years ended December 31, 2010, 2011 and 2012</u>                      | F-7         |
| <u>(f) Consolidated Statements of Cash Flows for the years ended December 31, 2010, 2011 and 2012</u>                  | F-8 F-9     |
| <u>(g) Notes to the consolidated financial statements</u>  | F-10 F-91   |

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**ITEM 19. EXHIBITS**

| <b>EXHIBIT</b> | <b>INDEX</b>  |
|----------------|---|
| 1.1            | Amended Memorandum and Articles of Association of our Company, incorporated by reference to Exhibit 1.3 to our annual report for the year 2006 on Form 20-F filed with the SEC on June 29, 2007 |
| 8.1            | List of Subsidiaries#   |
| 10.1           | Share Purchase Agreement among Infocomm Asia Holdings Pte. Ltd., GigaMedia Asia Pacific Limited, Management Capital International Limited, and Roland Ong Toon Wah dated July 2, 2012#          |
| 10.2           | Share Purchase Agreement among Infocomm Asia Holdings Pte. Ltd., GigaMedia Asia Pacific Limited, Spring Asia Limited and Roland Ong Toon Wah dated July 2, 2012#                                |
| 10.3           | Share Purchase Agreement between GigaMedia Capital Limited and Neowiz Corporation dated August 8, 2012#   |
| 12.1           | Certification by our Chief Executive Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act#   |
| 12.2           | Certification by our Chief Financial Officer pursuant to Rule 13a-14(b) of the Securities Exchange Act#   |
| 13.1           | Certification by our Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002#   |
| 13.2           | Certification by our Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002#   |
| 15.1           | Consent of GHP Horwath, P.C., Independent Registered Public Accounting Firm#  |

# Filed herewith.

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**SIGNATURE**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

**GIGAMEDIA LIMITED**

By: /s/ Collin Hwang  
Collin Hwang  
Chief Executive Officer  
Date: April 30, 2013

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**GHP Horwath, P.C.**  
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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Shareholders

GigaMedia Limited

We have audited the accompanying consolidated balance sheets of GigaMedia Limited and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of income (loss), comprehensive income (loss), equity, and cash flows for each of the three years in the period ended December 31, 2012. We also have audited the Company's internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A GHP Financial Group Company  
*GHP Horwath, P.C. is an independent member firm of Crowe Horwath International, a Swiss Verein. Each member firm of Crowe Horwath International is a separate and independent legal entity.*



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In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of GigaMedia Limited and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control Integrated Framework* issued by the COSO.

/s/ GHP HORWATH, P.C.

April 30, 2013

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GIGAMEDIA LIMITED  
 CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2011 AND 2012

(in thousands)

|   | December 31       |                   |
|---|-------------------|-------------------|
|   | 2011              | 2012              |
| <b>ASSETS</b>                                       |                   |                   |
| <b>CURRENT ASSETS</b>                               |                   |                   |
| Cash and cash equivalents (Note 11)                 | \$ 63,997         | \$ 62,731         |
| Marketable securities - current (Note 12)           | 42,347            | 17,773            |
| Accounts receivable - net (Note 13)                 | 6,451             | 2,829             |
| Prepaid expenses                                    | 1,574             | 801               |
| Restricted cash (Note 17)                           | 3,000             |                   |
| Other current assets (Notes 14 and 25)              | 1,551             | 1,001             |
| <b>Total Current Assets</b>                         | <b>118,920</b>    | <b>85,135</b>     |
| Marketable securities - noncurrent (Note 15)        | 7,084             | 4,292             |
| Investments (Note 16)                               | 8,315             | 5,223             |
| <b>PROPERTY, PLANT AND EQUIPMENT</b>                |                   |                   |
| Land and buildings                                  | 1,237             | 1,243             |
| Information and communication equipment             | 7,651             | 3,986             |
| Office furniture and fixtures                       | 928               | 295               |
| Leasehold improvements                              | 1,781             | 455               |
| Other   | 336               | 28                |
|   | 11,933            | 6,007             |
| Less: Accumulated depreciation                      | (7,645)           | (4,058)           |
|   | 4,288             | 1,949             |
| <b>GOODWILL (Note 7)</b>                            | <b>28,437</b>     | <b>16,934</b>     |
| <b>INTANGIBLE ASSETS - NET (Note 8)</b>             | <b>15,534</b>     | <b>15,675</b>     |
| <b>OTHER ASSETS</b>                                 |                   |                   |
| Refundable deposits                                 | 1,777             | 392               |
| Prepaid licensing and royalty fees (Notes 9 and 27) | 7,103             | 8,644             |
| Other (Note 6)                                      | 248               | 2,150             |
| <b>Total Other Assets</b>                           | <b>9,128</b>      | <b>11,186</b>     |
| <b>TOTAL ASSETS</b>                                 | <b>\$ 191,706</b> | <b>\$ 140,394</b> |

(Continued)



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## GIGAMEDIA LIMITED

## CONSOLIDATED BALANCE SHEETS - (Continued)

DECEMBER 31, 2011 AND 2012

(in thousands)

|  | December 31       |                   |
|--|-------------------|-------------------|
|  | 2011              | 2012              |
| <b><u>LIABILITIES &amp; EQUITY</u></b>   |                   |                   |
| <b>CURRENT LIABILITIES</b>   |                   |                   |
| Accounts payable   | \$ 1,831          | \$ 324            |
| Accrued compensation   | 2,100             | 1,233             |
| Accrued expenses (Note 18)   | 10,634            | 5,182             |
| Short-term borrowings (Notes 17 and 26)  | 11,774            | 7,748             |
| Other current liabilities (Note 19)  | 9,319             | 7,160             |
| Total Current Liabilities  | 35,658            | 21,647            |
| <b>OTHER LIABILITIES</b>   |                   |                   |
| Accrued pension liabilities (Note 20)  | 171               | 281               |
| Other (Notes 21 and 25)  | 1,015             | 573               |
| Total Other Liabilities  | 1,186             | 854               |
| Total Liabilities  | 36,844            | 22,501            |
| <b>COMMITMENTS AND CONTINGENCIES (Note 27)</b>   |                   |                   |
| <b>SUBSIDIARY PREFERRED SHARES (Note 22)</b>   |                   |                   |
| Par value \$1, redeemable; convertible; issued and outstanding 2,018 thousand shares on December 31, 2011                                | 1,786             |                   |
| <b>EQUITY (Note 23)</b>  |                   |                   |
| GigaMedia Shareholders' Equity:  |                   |                   |
| Common shares, no par value, and additional paid-in capital; issued and outstanding 50,720 thousand shares on December 31, 2011 and 2012 | 304,672           | 304,851           |
| Accumulated deficit  | (162,951)         | (178,241)         |
| Accumulated other comprehensive (loss) income  | 14,351            | (8,379)           |
| Total GigaMedia shareholders' equity   | 156,072           | 118,231           |
| Noncontrolling interest  | (2,996)           | (338)             |
| Total Equity   | 153,076           | 117,893           |
| <b>TOTAL LIABILITIES AND EQUITY</b>  | <b>\$ 191,706</b> | <b>\$ 140,394</b> |

The accompanying notes are an integral part of these consolidated financial statements.

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## GIGAMEDIA LIMITED

## CONSOLIDATED STATEMENTS OF INCOME (LOSS)

FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

(in thousands except for earnings per share amounts)

|   | 2010      | 2011     | 2012     |
|---|-----------|----------|----------|
| <b>OPERATING REVENUES</b>   |           |          |          |
| Gaming software and service revenues  | \$ 25,820 | \$       | \$       |
| Asian online game and service revenues  | 38,862    | 34,367   | 27,470   |
| Total   | 64,682    | 34,367   | 27,470   |
| <b>OPERATING COSTS</b>  |           |          |          |
| Cost of gaming software and service revenues  | (4,010)   |          |          |
| Cost of Asian online game and service revenues  | (17,103)  | (14,413) | (11,388) |
|   | (21,113)  | (14,413) | (11,388) |
| <b>GROSS PROFIT</b>   | 43,569    | 19,954   | 16,082   |
| <b>OPERATING EXPENSES</b>   |           |          |          |
| Product development and engineering expenses  | (7,301)   | (1,956)  | (1,471)  |
| Selling and marketing expenses  | (21,589)  | (10,079) | (8,377)  |
| General and administrative expenses   | (31,780)  | (18,101) | (13,384) |
| Bad debt expense (Notes 13 and 14)  | (1,639)   | (1,820)  | (169)    |
| Impairment loss on property, plant and equipment                                      | (278)     |          |          |
| Impairment loss on goodwill (Notes 7 and 10)  | (2,255)   | (5,097)  | (12,489) |
| Impairment loss on intangible assets (Note 10)  | (1,330)   | (2,583)  | (15)     |
| Impairment loss on prepaid licensing and royalty fees (Notes 9 and 10)                | (870)     | (247)    | (702)    |
| Impairment loss on deconsolidation of T2CN (Note 5)                                   | (22,234)  |          |          |
| Other   | (1,989)   |          | (49)     |
|   | (91,265)  | (39,883) | (36,656) |
| <b>LOSS FROM OPERATIONS</b>   | (47,696)  | (19,929) | (20,574) |
| <b>NON-OPERATING INCOME (EXPENSES)</b>  |           |          |          |
| Interest income   | 956       | 762      | 283      |
| Gain on sales of marketable securities (Notes 12 and 15)                              |           | 6,299    | 5,665    |
| Interest expense  | (370)     | (426)    | (247)    |
| Foreign exchange gain (loss)  | (606)     | (365)    | 434      |
| Loss on disposal of property, plant and equipment                                     | (125)     | (49)     | (208)    |
| Gain (loss) on equity method investments - net (Note 16)                              | (20,770)  | (47,869) | 234      |
| Gain on sale of T2CN (Note 5)   |           | 4,739    |          |
| Impairment loss on marketable securities and investments (Note 10)                    | (4,677)   | (13,327) | (1,193)  |
| Gain on deconsolidation and sale of the gaming software and service business (Note 6) | 79,140    |          | 2,480    |
| Recovery of loss on termination of third-party contract (Notes 4 and 10)              |           | 2,012    |          |
| Gain on fair value changes of warrant derivative (Note 10)                            | 2,595     |          |          |
| Other   | 221       | 518      | 201      |

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|   |          |             |             |
|---|----------|-------------|-------------|
|   | 56,364   | (47,706)    | 7,649       |
| INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES  | 8,668    | (67,635)    | (12,925)    |
| INCOME TAX (EXPENSE) BENEFIT (Note 25)  | (7,260)  | 245         | (671)       |
| INCOME (LOSS) FROM CONTINUING OPERATIONS  | 1,408    | (67,390)    | (13,596)    |
| LOSS FROM DISCONTINUED OPERATIONS - NET OF TAX (Note 6)   | (128)    | (4,188)     | (2,521)     |
| NET INCOME (LOSS)   | 1,280    | (71,578)    | (16,117)    |
| LESS: NET LOSS ATTRIBUTABLE TO THE NONCONTROLLING INTEREST AND<br>SUBSIDIARY PREFERRED SHARES           | 1,370    | 366         | 827         |
| NET INCOME (LOSS) ATTRIBUTABLE TO GIGAMEDIA   | \$ 2,650 | (\$ 71,212) | (\$ 15,290) |
| NET INCOME (LOSS) ATTRIBUTABLE TO GIGAMEDIA:  |          |             |             |
| Income (loss) from continuing operations - net of tax   | \$ 2,778 | (\$ 67,024) | (\$ 12,769) |
| Loss from discontinued operations - net of tax  | (128)    | (4,188)     | (2,521)     |
|   | \$ 2,650 | (\$ 71,212) | (\$ 15,290) |
| EARNINGS (LOSS) PER SHARE ATTRIBUTABLE TO GIGAMEDIA   |          |             |             |
| Basic:  |          |             |             |
| Income (loss) from continuing operations  | \$ 0.05  | (\$ 1.23)   | (\$ 0.25)   |
| Loss from discontinued operations   |          | (0.08)      | (0.05)      |
| Net income (loss)   | \$ 0.05  | (\$ 1.31)   | (\$ 0.30)   |
| Diluted:  |          |             |             |
| Income (loss) from continuing operations  | \$ 0.04  | (\$ 1.23)   | (\$ 0.25)   |
| Loss from discontinued operations   |          | (0.08)      | (0.05)      |
| Net income (loss)   | \$ 0.04  | (\$ 1.31)   | (\$ 0.30)   |
| WEIGHTED AVERAGE SHARES USED TO COMPUTE EARNINGS (LOSS) PER SHARE<br>ATTRIBUTABLE TO GIGAMEDIA (Note 2) |          |             |             |
| Basic   | 55,834   | 54,268      | 50,720      |
| Diluted   | 59,291   | 54,268      | 50,720      |

The accompanying notes are an integral part of these consolidated financial statements.

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## GIGAMEDIA LIMITED

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

FOR THE YEARS DECEMBER 31, 2010, 2011 AND 2012

(in thousands)

|   | 2010      | 2011        | 2012        |
|---|-----------|-------------|-------------|
| NET INCOME (LOSS)   | \$ 1,280  | (\$ 71,578) | (\$ 16,117) |
| OTHER COMPREHENSIVE INCOME - NET OF TAX:  |           |             |             |
| Unrealized gain (loss) on marketable securities   | 21,789    | 16,167      | (24,004)    |
| Defined benefit pension plan adjustment   | 31        | 69          | (323)       |
| Foreign currency translation adjustments  | 4,756     | (1,813)     | 1,814       |
| Deconsolidation of subsidiaries   | (1,311)   |             | 2,799       |
|   | 25,265    | 14,423      | (19,714)    |
| COMPREHENSIVE INCOME (LOSS)   | 26,545    | (57,155)    | (35,831)    |
| COMPREHENSIVE (INCOME) LOSS ATTRIBUTABLE TO THE NONCONTROLLING INTEREST AND SUBSIDIARY PREFERRED SHARES | 1,278     | 366         | (2,189)     |
| COMPREHENSIVE INCOME (LOSS) ATTRIBUTABLE TO GIGAMEDIA   | \$ 27,823 | (\$ 56,789) | (\$ 38,020) |

The accompanying notes are an integral part of these consolidated financial statements.

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## GIGAMEDIA LIMITED

## CONSOLIDATED STATEMENTS OF EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

(in thousands, except per share amounts)

|  | GIGAMEDIA SHAREHOLDERS                                    |            |                                     |   |                            |            |
|--|---|------------|-------------------------------------|---|----------------------------|------------|
|  | Common shares<br>and additional paid-in capital<br>Shares | Amount     | Accumulated<br>deficit<br>(Note 23) | Accumulated other<br>comprehensive<br>income (loss) | Noncontrolling<br>interest | Total      |
| Balance as of January 1, 2010  | 54,995  | \$ 304,379 | (\$ 94,389)                         | (\$ 25,245)   | \$ 1,615                   | \$ 186,360 |
| Issuance of common shares from exercise of stock options and RSUs        | 402   | 174        |                                     |   |                            | 174        |
| Stock-based compensation   |   | 2,961      |                                     |   | 53                         | 3,014      |
| Acquisition of IAHGames (Note 4)   | 866   | 2,192      |                                     |   | 1,192                      | 3,384      |
| Acquisition of UIM (Note 3)  |   | 178        |                                     |   | (578)                      | (400)      |
| Deconsolidation of T2CN (Note 5)   |   | (552)      |                                     |   | (3,276)                    | (3,828)    |
| Cumulative dividend to subsidiary preferred shares (Note 22)             |   |            |                                     |   | (148)                      | (148)      |
| Net income   |   |            | 2,650                               |   | (1,370)                    | 1,280      |
| Components of other comprehensive income (loss):                         |   |            |                                     |   |                            |            |
| Change in unrealized gain (loss) on marketable securities                |   |            |                                     | 21,789  |                            | 21,789     |
| Defined benefit pension plan adjustment                                  |   |            |                                     | 31  |                            | 31         |
| Foreign currency translation adjustments                                 |   |            |                                     | 4,744   | 12                         | 4,756      |
| Deconsolidation of T2CN (Note 5)   |   |            |                                     | (1,391)   | 80                         | (1,311)    |
| Total comprehensive income   |   |            |                                     |   |                            | 26,545     |
| Balance as of December 31, 2010  | 56,263  | 309,332    | (91,739)                            | (72)  | (2,420)                    | 215,101    |
| Issuance of common shares from exercise of stock options and RSUs        | 79  |            |                                     |   |                            |            |
| Stock-based compensation   |   | 1,165      |                                     |   |                            | 1,165      |
| Acquisition of OneNet  |   |            |                                     |   | 111                        | 111        |
| Share repurchase and retirement of common shares (Note 23)               | (5,622)   | (5,825)    |                                     |   |                            | (5,825)    |
| Cumulative dividend to subsidiary preferred shares (Note 22)             |   |            |                                     |   | (321)                      | (321)      |
| Net loss   |   |            | (71,212)                            |   | (366)                      | (71,578)   |
| Components of other comprehensive income (loss):                         |   |            |                                     |   |                            |            |
| Change in unrealized gain (loss) on marketable securities                |   |            |                                     | 16,167  |                            | 16,167     |
| Defined benefit pension plan adjustment                                  |   |            |                                     | 69  |                            | 69         |
| Foreign currency translation adjustments                                 |   |            |                                     | (1,813)   |                            | (1,813)    |
| Total comprehensive loss   |   |            |                                     |   |                            | (57,155)   |
| Balance as of December 31, 2011  | 50,720  | 304,672    | (162,951)                           | 14,351  | (2,996)                    | 153,076    |
| Stock-based compensation   |   | 179        |                                     |   |                            | 179        |
| Reversal of cumulative dividend to subsidiary preferred shares (Note 22) |   |            |                                     |   | 469                        | 469        |
| Net loss   |   |            | (15,290)                            |   | (827)                      | (16,117)   |



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|   |        |            |              |            |          |            |          |
|---|--------|------------|--------------|------------|----------|------------|----------|
| Components of other comprehensive income (loss):          |        |            |              |            |          |            |          |
| Change in unrealized gain (loss) on marketable securities |        |            |              | (24,004)   |          |            | (24,004) |
| Defined benefit pension plan adjustment                   |        |            |              | (323)      |          |            | (323)    |
| Foreign currency translation adjustments                  |        |            |              | 1,814      |          |            | 1,814    |
| Deconsolidation of IAHGames (Note 6)                      |        |            |              | (217)      | 3,016    |            | 2,799    |
| Total comprehensive loss                                  |        |            |              |            |          |            | (35,831) |
| Balance as of December 31, 2012                           | 50,720 | \$ 304,851 | (\$ 178,241) | (\$ 8,379) | (\$ 338) | \$ 117,893 |          |

The accompanying notes are an integral part of these consolidated financial statements.

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## GIGAMEDIA LIMITED

## CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

(in thousands)

|   | 2010     | 2011        | 2012        |
|---|----------|-------------|-------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |          |             |             |
| Net income (loss)   | \$ 1,280 | (\$ 71,578) | (\$ 16,117) |
| Adjustments to reconcile net income (loss) to net cash used in operating activities:            |          |             |             |
| Depreciation  | 2,092    | 2,080       | 1,224       |
| Amortization  | 2,779    | 2,314       | 2,204       |
| Stock-based compensation  | 3,014    | 1,165       | 179         |
| Gain on deconsolidation and sale of gaming software and service business                        | (79,140) |             | (2,480)     |
| Impairment loss on property, plant and equipment  | 278      |             |             |
| Impairment loss on goodwill   | 2,255    | 5,097       | 12,489      |
| Impairment loss on intangible assets  | 1,330    | 2,583       | 15          |
| Impairment loss on prepaid licensing and royalty fees   | 870      | 247         | 702         |
| Provision for bad debt expenses   | 1,639    | 1,820       | 169         |
| Loss on disposal of property, plant and equipment   | 125      | 49          | 208         |
| Gain on sales of marketable securities  |          | (6,299)     | (5,665)     |
| Gain on sale of T2CN  |          | (4,739)     |             |
| Loss (gain) on equity method investments  | 20,770   | 47,869      | (234)       |
| Impairment loss on marketable securities and investments  | 4,677    | 13,327      | 1,193       |
| Impairment loss on deconsolidation of T2CN  | 22,234   |             |             |
| Gain on cancellation of warrant liabilities   |          | (665)       |             |
| Gain on fair value changes of warrant derivative  | (2,595)  |             |             |
| Other   | (125)    | 200         | 377         |
| Net changes in operating assets and liabilities, net of business acquisitions and divestitures: |          |             |             |
| Accounts receivable   | 3,263    | (153)       | 1,537       |
| Prepaid expenses  | (2,992)  | 871         | 755         |
| Other current assets  | 2,215    | 865         | (174)       |
| Accounts payable  | 1,867    | (336)       | (515)       |
| Accrued expenses  | 3,519    | (452)       | (59)        |
| Accrued compensation  | 1,667    | (2,139)     | (831)       |
| Player account balances   | 229      |             |             |
| Other current liabilities   | 4,568    | (1,334)     | (467)       |
| Accrued pension liabilities   | (39)     | 128         | 110         |
| Prepaid licensing and royalty fees  | (3,855)  | (3,007)     | (2,397)     |
| Other   | (847)    | (361)       | 454         |
| Net cash used in operating activities   | (8,922)  | (12,448)    | (7,323)     |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |          |             |             |
| Decrease (increase) in restricted cash  | (4,068)  | 2,000       | 3,694       |
| Cash dividends received from equity method investees  | 945      | 1,907       |             |
| Proceeds from disposal of marketable securities   |          | 9,899       | 8,610       |
| Divestiture of business, net of cash transferred  |          | 4,739       | (1,308)     |
| Purchase of property, plant and equipment   | (3,784)  | (768)       | (429)       |
| Proceeds from disposal of property, plant and equipment   | 119      | 117         | 76          |
| Proceeds from disposal of businesses, net of transaction costs                                  | 85,669   |             | 1,735       |
| Purchase of marketable securities   | (1,500)  |             |             |
| Purchase of investments   | (5,261)  |             |             |

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|  |          |         |         |
|--|----------|---------|---------|
| Purchase of intangible assets              | (2,317)  | (1,274) | (1,679) |
| Acquisitions, net of cash acquired         | (5,831)  | 11      |         |
| Advances to equity investees               | (13,804) | (5,243) |         |
| Decrease (increase) in refundable deposits | (146)    | 185     | 428     |
| Other                                      |          | (22)    | (10)    |
| Net cash provided by investing activities  | 50,022   | 11,551  | 11,117  |

(Continued)

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## GIGAMEDIA LIMITED

## CONSOLIDATED STATEMENTS OF CASH FLOWS - (Continued)

FOR THE YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

(in thousands)

|   | 2010             | 2011             | 2012             |
|---|------------------|------------------|------------------|
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                              |                  |                  |                  |
| Net repayment of short-term borrowings                                    | (12,543)         | (400)            | (4,348)          |
| Repurchase and retirement of common shares                                |                  | (5,825)          |                  |
| Cash received from the exercise of stock options                          | 174              |                  |                  |
| Other   | 5                |                  |                  |
| Net cash used in financing activities                                     | (12,364)         | (6,225)          | (4,348)          |
| Exchange difference   | (410)            | 130              | (712)            |
| Deconsolidation of T2CN   | (12,903)         |                  |                  |
| <b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>               | <b>15,423</b>    | <b>(6,992)</b>   | <b>(1,266)</b>   |
| <b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>                     | <b>55,566</b>    | <b>70,989</b>    | <b>63,997</b>    |
| <b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>                           | <b>\$ 70,989</b> | <b>\$ 63,997</b> | <b>\$ 62,731</b> |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>                 |                  |                  |                  |
| Interest paid during the year   | \$ 313           | \$ 436           | \$ 248           |
| Income tax paid during the year   | \$ 3,799         | \$ 783           | \$ 121           |
| <b>NON-CASH FINANCING AND INVESTING ACTIVITIES:</b>                       |                  |                  |                  |
| Change in unrealized holding gain (loss) on available-for-sale securities | \$ 21,789        | \$ 16,167        | (\$ 24,004)      |
| Issuance of common shares for acquisition                                 | \$ 2,192         | \$               | \$               |
| Transfer of marketable securities from current to non-current             | \$               | \$ 42,347        | \$               |

The accompanying notes are an integral part of these consolidated financial statements.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 1. BUSINESS OVERVIEW, BASIS OF PRESENTATION, AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*(a) Business Overview*

GigaMedia Limited (referred to hereinafter as GigaMedia, our Company, we, us, or our) is a provider of online entertainment software and services, with headquarters in Taipei, Taiwan. In the second half year of 2012, we also began developing the business of providing cloud computing services, which launched in March 2013.

Through July 31, 2012, we conducted our online entertainment business in two business segments: the gaming software and service business, which develops and licenses software for online real-money gaming solutions and applications; and the Asian online game and service business, which develops a wide range of online games for the Asian and worldwide market.

In April 2010, we sold a 60 percent interest in our online gaming software and service business to Mangas Gaming S.A.S., a French Corporation, now renamed as BetClic Everest Group ( BEG ). Our retained non-controlling interest in the online gaming software and service business was sold to BEG in July 2012. (See Note 6, Divestitures , for additional information.)

Our gaming software and service business developed and licensed online poker and casino gaming software solutions and application services, primarily targeting continental European markets. Prior to our disposal of the remaining ownership, through our equity investment, the gaming software and service business offered software solutions for online gaming, which was licensed under a software license and support service contract.

Our Asian online game and service business operates a suite of play-for-fun online games and provides related services, mainly targeting online game players across Asia, including Greater China and Southeast Asia.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

We began developing a new cloud computing business in the second half of 2012. The cloud business aims at providing an integrated platform of services and tools for small-to-medium enterprises in Greater China to increase flexibility, efficiency and competitiveness. The business launched in late March 2013.

***(b) Basis of Presentation***

The gaming software and service business does not qualify as a component that may be reported as discontinued operations due to our significant continuing involvement in the component after the initial disposal of our 60 percent interest in 2010. After the sale transaction was completed in April 2010, we deconsolidated the results of the gaming software and service business and began accounting for the remaining interest under the equity method of accounting until the closing of the disposal transaction in July 2012 when we sold our remaining ownership. (See Note 6, *Divestitures*, for additional information.)

***Discontinued Operations***

In June 2012, our board of directors approved a plan to liquidate and dissolve JIDI Network Technology (Shanghai) Co., Ltd. ( *JIDI* ), a wholly-owned subsidiary, and Shanghai JIDI Network Technology Co., Ltd. ( *Shanghai JIDI* ), a variable-interest entity controlled through a series of contractual arrangements. Therefore the results of these entities are reported as discontinued operations for all periods presented. (See Note 6, *Divestitures*, for additional information.)

***Principles of Consolidation***

The Consolidated Financial Statements include the accounts of GigaMedia and our wholly-owned, majority-owned and majority-controlled subsidiaries after elimination of all inter-company accounts and transactions. In addition, the accounts of our Company's variable-interest entities ( *VIE* ), as defined by the Financial Accounting Standards Board ( *FASB* ), are included in the Consolidated Financial Statements. (See Note 3, *Variable-Interest Entities*, for additional information.) The accounting policies for other less than majority-owned investments are described in Note 1 below within the paragraphs headed *Marketable Securities* and *Investments*.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***Foreign Currency Translation***

The Consolidated Financial Statements of our Company and our subsidiaries have been reported in U.S. dollars. Assets and liabilities denominated in non-U.S. currency are translated to U.S. dollars at year-end exchange rates. Income and expense items are translated at weighted-average rates of exchange prevailing during the year. Cumulative translation adjustments resulting from this process are charged or credited to other comprehensive income within equity. Gains and losses on foreign currency transactions are included in other income and expenses. Cumulative translation adjustments as of December 31, 2010, 2011 and 2012 were \$(22.6) million, \$(24.4) million, and \$(22.8) million, respectively.

***(c) Summary of significant accounting policies***

***Use of Estimates***

The preparation of Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States of America ( GAAP ) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the dates of the Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

***Revenue Recognition***

**General**

Our Company recognizes revenues when persuasive evidence of an arrangement exists, delivery occurs or services are rendered, the sales price is fixed or determinable and collectability is reasonably assured.

We present the sales taxes assessed by governmental authorities on our revenue transactions on a net basis in our Consolidated Financial Statements.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Multiple-Element Arrangements**

Our Company enters into multiple-element revenue arrangements, which may include any combination of services, software, and/or products. To the extent that a deliverable in a multiple-element arrangement is subject to specific accounting guidance, whether and/or how to separate multiple deliverable arrangements into separate units of accounting (separability) and how to allocate the arrangement consideration among those separate units of accounting (allocation) for that deliverable is accounted for in accordance with such specific guidance.

In addition to the aforementioned general policies, the following are the specific revenue recognition policies for each major category of revenue.

**Asian Online Game and Service Revenues**

Asian online game and service revenues are related to our Asian online game and service business that operates play-for-fun games online to players across Asia.

Online game revenues are earned through the sale of online game points, prepaid cards, game packs, through the sublicensing of certain games to distributors and through licensing fee revenues. Virtual online game points are sold to distributors or end-users who can make the payments through credit cards, Internet ATMs or telecommunication service operators. Physical prepaid cards and game packs are sold through distributors and convenience stores. Proceeds from sales of physical cards and game packs, net of sales discounts, and online game points are deferred when received and revenue is recognized upon the actual usage of the playing time or in-game virtual items by the end-users; over the estimated useful life of virtual items; or when the sold game points expire and can no longer be used to access the online games or products in accordance with our published game points expiration policy. Sublicensing revenues from the distributors are recognized based on end-users activation to the game system and when the performance obligations have been completed. Licensing fee revenues are recognized when the delivery of licensed products has occurred and the fee is fixed or determinable.



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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

We report sales of virtual online game points and licensing fee revenues on a gross basis. In the sales of virtual online game points and game licenses, we act as principal and we have latitude in establishing price. Fixed percentage fees retained by service providers for payment processing related to our online game services are recognized as cost of online game revenues. We report sublicensing revenues on a net basis. In the sublicense agreements, we act as agent and the distributors are responsible for the operating and the marketing.

Online game and service revenues also include revenues derived from online advertising arrangements, sponsorship arrangements, or a combination of both. These service arrangements allow advertisers to place advertisements on particular areas of our Company's websites and online game platforms over a stated period of time. Service revenues from online advertising arrangements are recognized ratably over the displayed period of the contract when the collectability is reasonably assured.

**Gaming Software and Service Revenues**

Prior to our sale of a majority interest in the online gaming software and service business in April 2010, gaming software and service revenues were related to software products we developed and licensed and support services we provided for online real-money gaming solutions and applications.

**Deferred Revenues**

Deferred revenues are included in other current liabilities, and consist of the prepaid income related to our Asian online game and service business.

**Operating Costs**

Operating costs primarily consist of processing costs, online game royalties, bandwidth, production costs for prepaid game cards and game packs, amortization of intangible assets, customer service department costs, depreciation, maintenance and other overhead expenses directly attributable to our online games.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***Prepaid Licensing and Royalty Fees***

Our Company, through our subsidiaries, routinely enters into agreements with licensors to acquire licenses for using, marketing, distributing, selling and publishing multi-player online games.

Prepaid licensing fees paid to licensors are capitalized when technological feasibility is achieved, and amortized on a straight-line basis over the shorter of the estimated useful economic life of the relevant online game or license period, which is usually within two to five years. The annual amortization is modified if the amount computed using the ratio that current gross revenues for a game license bear to the total of current and anticipated future gross revenues for that game license is greater than the amount computed using the straight-line method.

Prepaid royalty fees and related costs are initially deferred when paid to licensors and recognized as operating costs in the period in which the related online game revenue is recognized.

***Fair Value Measurements***

Our Company generally determines or calculates the fair value of financial instruments using quoted market prices in active markets when such information is available or using appropriate present value or other valuation techniques, such as discounted cash flow analyses, incorporating adjusted available market discount rate information and our Company's estimates for non-performance and liquidity risk. These techniques rely extensively on the use of a number of assumptions, including the discount rate, credit spreads, and estimates of future cash flows. (See Note 10, Fair Value Measurements, for additional information.)

***Cash Equivalents***

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and so near to their maturity that they present relatively insignificant risk from changes in interest rates. Commercial paper, negotiable certificates of deposit, time deposits and bank acceptances with original maturities of three months or less are considered to be cash equivalents.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***Marketable Securities***

All of our Company's investments in marketable securities are classified as available-for-sale. These marketable securities are stated at fair value with any unrealized gains or losses recorded in accumulated other comprehensive income (loss) within equity until realized.

Other-than-temporary impairments, if any, are charged to non-operating expense in the period in which the loss occurs. In determining whether an other-than-temporary impairment has occurred, our Company primarily considers, among other factors, the length of the time and the extent to which the fair value of an investment has been at a value less than cost. When an other-than-temporary loss is recorded, the fair value of the investment becomes the new cost basis of the investment and is not adjusted for subsequent recoveries in fair value. Realized gains and losses also are included in non-operating income and expense in the Consolidated Statements of Income (Loss). (See Note 10, Fair Value Measurements, for additional information.)

***Investments***

Equity investments in non-publicly traded securities of companies over which our Company has no ability to exercise significant influence are accounted for under the cost method.

Equity investments in companies over which our Company has the ability to exercise significant influence but does not hold a controlling financial interest are accounted for under the equity method and our Company's income or loss on equity method investments is recorded in non-operating income or expenses. The difference between the cost of the acquisition and our Company's share of the fair value of the net identifiable assets is recognized as goodwill and is included in the carrying amount of the investment. When our Company's carrying value in an equity method investee is reduced to zero, no further losses are recorded in our Consolidated Financial Statements unless our Company guaranteed obligations of the investee or has committed to additional funding. When the investee subsequently reports income, our Company will not record its share of such income until it equals the amount of its share of losses not previously recognized.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Unrealized losses that are considered other-than-temporary, if any, are charged to non-operating expenses. Realized gains and losses, measured against carrying amount, are also included in non-operating income and expenses. (See Note 10, Fair Value Measurements, for additional information.)

***Allowance for Doubtful Accounts***

An allowance for doubtful accounts is provided based on an evaluation of the collectability of accounts receivable, and other receivables. An allowance for doubtful accounts is also provided, when considered necessary, for loans receivable. We review the collectability of loans receivable on an individual basis and the evaluation primarily consists of an analysis based upon current information available about the borrower.

For those accounts in which a loss is probable, we record a specific reserve in the allowance. The receivable is written off against the allowance when our Company believes the uncollectability of the receivable is confirmed. Subsequent recoveries, if any, are credited to the allowance.

***Property, Plant and Equipment***

Property, plant and equipment are stated at cost, less accumulated depreciation. Depreciation is provided on a straight-line basis over useful lives that correspond to categories as follows:

| Categories                              | Years  |
|---|--------|
| Buildings                               | 50     |
| Information and communication equipment | 2 to 5 |
| Office furniture and equipment          | 3 to 5 |
| Leasehold improvements                  | 3 to 5 |

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Leasehold improvements are depreciated over the shorter of the term of the lease or the economic useful life of the assets. Improvements and replacements are capitalized and depreciated over their estimated useful lives, while ordinary repairs and maintenance are expensed as incurred.

We have entered into agreements to lease certain of our Company's land and buildings to a third party under operating leases, which were renewed in November 2012, and which expire no later than September 2013. As of December 31, 2011 and 2012, the carrying amount of the land and buildings under lease was approximately \$1.3 million and \$1.2 million, respectively. The rental income under the operating lease amounted to \$41 thousand, \$72 thousand and \$74 thousand for 2010, 2011 and 2012, respectively. The minimum rental income to be received under this operating lease is \$53 thousand through September 2013.

***Acquisitions***

Our Company accounts for its business acquisitions using the acquisition method. Under this method, our Company recognizes and measures the identifiable assets acquired, the liabilities assumed and any noncontrolling interest at their acquisition-date fair values, with limited exceptions. Acquisition-related costs are generally expensed as incurred.

***Intangible Assets and Goodwill***

Intangible assets with finite lives are amortized by the straight-line method over their estimated useful lives, ranging from three to nine years. Intangible assets with indefinite useful lives are not amortized. Goodwill is not amortized.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***Impairment of Intangible Assets, Goodwill and Long-Lived Assets***

Goodwill is tested for impairment annually or sooner when circumstances indicate an impairment may exist, using a fair-value approach at the reporting unit level. A reporting unit is the operating segment, or a business, which is one level below that operating segment (the component level) if discrete financial information is prepared and regularly reviewed by management at the segment level. Components are aggregated as a single reporting unit if they have similar economic characteristics. In connection with our goodwill impairment test, we first assess qualitative factors as a basis for determining whether it is necessary to perform the two-step goodwill impairment test.

Intangible assets with indefinite useful lives are tested for impairment at the reporting unit level, at least annually, or whenever events or changes in circumstances indicate that the carrying value of an asset might not be recoverable from its related future discounted cash flows. Impairment is measured as the difference between the carrying amounts and the fair value of the assets, and is recognized as a loss from operations. In connection with our impairment test for the intangible assets with indefinite useful lives, we first assess qualitative factors as a basis for determining whether it is necessary to perform the quantitative impairment test.

Long-lived assets other than goodwill and intangible assets not being amortized are tested for impairment at least annually or whenever events or changes in circumstances indicate that the carrying value of an asset might not be recoverable from its related future undiscounted cash flows. If such assets are considered to be impaired, the impairment to be recognized is measured by the extent to which the carrying amount of the assets exceeds the fair value of the assets. When impairment is identified, the carrying amount of the asset is reduced to its estimated fair value, and is recognized as a loss from operations.

(See Note 10, Fair Value Measurements , for additional information.)

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***Software Cost***

Costs to develop our gaming software and Asian online game products are capitalized after technological feasibility has been established, and when the product is available for general release to customers, costs are expensed. Costs incurred prior to the establishment of technological feasibility are expensed when incurred and are included in product development and engineering expenses. Capitalized amounts are amortized using the straight-line method, which is applied over the estimated useful economic life of the software, ranging from three to five years. The annual amortization is modified if the amount computed using the ratio that current gross revenues for a product bear to the total of current and anticipated future gross revenues for that product is greater than the amount computed using the straight-line method.

We capitalize certain costs incurred to purchase or to internally create and implement internal-use computer software, which includes software coding, installation, testing and certain data conversion. These capitalized costs are amortized on a straight-line basis over the shorter of the useful economic life of the software or its contractual license period, which range from three to five years.

***Product Development and Engineering***

Product development and engineering expenses primarily consist of research compensation, depreciation and amortization, and are expensed as incurred.

***Advertising***

Direct-response advertising costs incurred in relation to the acquisition or origination of a customer relationship are capitalized and deferred. The deferred costs are recognized as expense in the Consolidated Statements of Income (Loss) over the estimated lives of customer relationships. Costs of broadcast advertising are recorded as expenses as advertising airtime is used. Other advertising expenditures are expensed as incurred. Subsequent to the sale of a majority interest in the online gaming and software service business in April 2010, deferred costs related to advertising have not been significant.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Advertising expenses incurred in 2010, 2011 and 2012 totaled \$12.7 million, \$3.5 million and \$3.2 million, respectively. As of December 31, 2011 and 2012, prepaid advertising amounted to \$110 thousand and \$1 thousand, respectively.

***Leases***

Leases for which substantially all of the risks and rewards of ownership remain with the leasing company are accounted for as operating leases. Payments made under operating leases, net of any incentives received by our Company from the leasing company, are charged to the Consolidated Statements of Income (Loss) on a straight-line basis over the lease periods.

Leases are classified as capital leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. Assets held under capital leases are recognized as assets of our Company at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a lease obligation. Lease payments are apportioned between finance charges and a reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss.

***Share-Based Compensation***

Share-based compensation represents the cost related to share-based awards granted to employees. We measure share-based compensation cost at the grant date, based on the estimated fair value of the award. Share-based compensation is recognized for the portion of the award that is ultimately expected to vest, and the cost is amortized on a straight-line basis (net of estimated forfeitures) over the vesting period. Our Company estimates the fair value of stock options using the Black-Scholes valuation model. The cost is recorded in operating costs and operating expenses in the Consolidated Statements of Income (Loss) based on the employees' respective function.



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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

For shares and stock options granted to non-employees, we measure the fair value of the equity instruments granted at the earlier of the performance commitment date or when the performance is completed.

***Retirement Plan and Net Periodic Pension Cost***

Under our defined benefit pension plan, net periodic pension cost, which includes service cost, interest cost, expected return on plan assets, amortization of unrecognized net transition obligation and gains or losses on plan assets, is recognized based on an actuarial valuation report. We recognize the funded status of pension plans and non-pension post-retirement benefit plans (retirement-related benefit plans) as an asset or a liability in the Consolidated Balance Sheets.

Under our defined contribution pension plans, net periodic pension cost is recognized as incurred.

***Comprehensive Income (Loss)***

Comprehensive income (loss) is recorded as a component of equity. Our Company's comprehensive income (loss) consists of net income or loss, foreign currency translation adjustments, changes in unrealized holding gains and losses on marketable securities, and unrecognized actuarial gains or losses related to our defined benefit pension plan.

***Income Taxes***

The asset and liability method is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on the differences between financial reporting and tax bases of assets and liabilities. We recognize the tax benefit from the purchase of equipment and technology, research and development expenditures, employee training, and certain equity investments using the flow-through method. Net operating loss carryforwards and investment credits are measured using the enacted tax rate and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established when necessary to reduce deferred tax assets to the amount that will more-likely-than-not be realized. In assessing the likelihood of realization, management considers estimates of future taxable income.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In addition, we recognize the financial statement impact of a tax position when it is more-likely-than-not that the position will be sustained upon examination. If the tax position meets the more-likely-than-not recognition threshold, the tax effect is recognized at the largest amount of the benefit that has greater than a 50 percent likelihood of being realized upon ultimate settlement. The interest and penalties are reflected as income tax expense in the Consolidated Financial Statements.

***Earnings Per Share***

Basic earnings per share is computed by dividing the net income available to common shareholders for the period by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing the net income for the period by the weighted average number of common shares and potential common shares outstanding during the period. Potential common shares, composed of incremental common shares issuable upon the exercise of warrants and options in all periods, are included in the computation of diluted earnings per share to the extent such shares are dilutive. Diluted EPS also takes into consideration the effect of dilutive securities issued by subsidiaries. In a period in which a loss is incurred, only the weighted average number of common shares issued and outstanding is used to compute the diluted loss per share, as the inclusion of potential common shares would be anti-dilutive. Therefore, for the years ended December 31, 2011 and 2012, basic and diluted loss per share are the same.

***Noncontrolling Interest***

Noncontrolling interest in the equity of a subsidiary is accounted for and reported as equity. Changes in our Company's ownership interest in a subsidiary that do not result in deconsolidation are accounted for as equity transactions. Any retained noncontrolling equity investment upon the deconsolidation of a subsidiary is initially measured at fair value.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***Reclassifications***

The presentation of certain amounts in our 2011 Consolidated Financial Statements have been reclassified to conform to the presentation in our Consolidated Financial Statements as of and for the year ended December 31, 2012.

***Recent Accounting Pronouncements***

In February 2013, Accounting Standards Update ( ASU ) guidance was issued related to items reclassified from Accumulated Other Comprehensive Income. The new standard requires either in a single note or parenthetically on the face of the financial statements:(i) the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and (ii) the income statement line items affected by the reclassification. The update is effective for our fiscal year beginning January 1, 2013 with early adoption permitted. We do not expect the updated guidance to have a significant impact on our consolidated financial position, results of operations or cash flows.

In July 2012, the FASB issued updated guidance that simplifies the impairment test for intangible assets not subject to amortization. For its annual and interim impairment test for intangible assets, an entity may first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the quantitative impairment test. This update is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. However, early adoption is permitted, if an entity's financial statements for the most recent annual or interim period have not yet been issued. We adopted the updated guidance for our annual impairment test for intangible assets not subject to amortization in 2012. The adoption of this guidance had no impact on our consolidated financial position, results of operations, or cash flows.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In June 2011, the ASU guidance was issued related to comprehensive income. Under the updated guidance, an entity will have the option to present the total of comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In addition, the update required certain disclosure requirements when reporting other comprehensive income. The update does not change the items reported in other comprehensive income or when an item of other comprehensive income must be reclassified to income. We adopted the new guidance and its deferral and opted to present the total of comprehensive income in two separate but consecutive statements. The adoption of this guidance had no impact on our consolidated financial position, results of operations or cash flows.

**NOTE 2. EARNINGS PER SHARE**

The following table provides a reconciliation of the denominators of the basic and diluted per share computations:

| (in thousand shares)                                 | 2010          | 2011          | 2012          |
|--|---------------|---------------|---------------|
| <b>Weighted average number of outstanding shares</b> |               |               |               |
| Basic  | 55,834        | 54,268        | 50,720        |
| Effect of dilutive securities                        |               |               |               |
| Employee share-based compensation                    | 3,457         |               |               |
| <b>Diluted</b>                                       | <b>59,291</b> | <b>54,268</b> | <b>50,720</b> |

Options to purchase 1,432 thousand and 1,444 thousand shares of common stock were not included in dilutive securities for the years ended December 31, 2011 and 2012, respectively, as the effect would be anti-dilutive.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 3. VARIABLE-INTEREST ENTITIES****Shanghai JIDI**

In order to comply with foreign ownership restrictions and to hold the necessary licenses required, through June 2012 we operated our Asian online game and service business in the People's Republic of China ( PRC ) through our VIE, Shanghai JIDI. We had no ownership interest in Shanghai JIDI and relied on a series of contractual arrangements that were intended to give us effective control over Shanghai JIDI. Those contractual arrangements were duly executed and the share pledge agreements were registered with local government authority in compliance with PRC legal requirements. In June 2012, our board of directors approved a plan to dispose of Shanghai JIDI. As a result, Shanghai JIDI's operations have been accounted for as discontinued operations. (See Note 6, "Divestitures", for additional information.) Therefore, we still effectively control Shanghai JIDI, and are therefore the primary beneficiary of Shanghai JIDI. Shanghai JIDI was established in December, 2010 and is effectively controlled by us through a series of contractual arrangements. Shanghai JIDI holds an Internet Content Provider ( ICP ) license, an Internet cultural operation license and an Internet publishing license. The financial results of Shanghai JIDI have been included in our consolidated financial statements since January 2011.

For the years ended December 31, 2011 and 2012, total revenues and net loss of Shanghai JIDI (which are included within discontinued operations) were as follows:

| (in US\$ thousands) | 2011       | 2012     |
|---------------------|------------|----------|
| Total revenues      | \$ 29      | \$ 100   |
| Net loss            | \$ (2,110) | \$ (888) |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Ultra Internet Media, S.A. ( UIM )**

Through the date of our sale of a majority interest in the gaming software and service business to BEG in April 2010, we had a software license and support service contract with UIM to provide Internet software and support services for UIM's online gaming operations. The contract allowed us to charge UIM a percentage of its gross receipts resulting from UIM's online gaming operations. The percentage of gross receipts varied depending upon the software and support services provided to UIM. We analyzed our contractual relationships with UIM and determined that we were the primary beneficiary of UIM. As a result of such determination, we had incorporated the financial results of UIM into our Consolidated Financial Statements, even though we did not own any of UIM's equity. In connection with the sale to BEG, we purchased 100 percent of the ownership in UIM from its shareholders for \$400 thousand and adjusted additional paid-in capital and noncontrolling interest by approximately \$178 thousand and \$(578) thousand, respectively.

For the period from January to March 2010, total revenues and net income of UIM were as follows:

|                     |           |
|---------------------|-----------|
| (in US\$ thousands) | 2010      |
| Total revenues      | \$ 25,820 |
| Net income          | \$ 1,514  |

**T2CN Holding Limited ( T2CN )**

Pursuant to various agreements entered into among Shanghai T2 Entertainment Co., ( T2 Entertainment ), T2 Information Technology (Shanghai) Co., Ltd. ( T2 Technology ) and the equity interest owners of T2 Entertainment, until June 30, 2010, T2CN, through its wholly owned subsidiary T2 Technology, had effective control over T2 Entertainment and was considered the primary beneficiary of T2 Entertainment. T2 Entertainment was established to hold the necessary licenses required for the operation of our Asian online game and services business in the PRC. Accordingly, from the date that we consolidated T2CN through July 1, 2010, the date we deconsolidated T2CN (See Note 5, Deconsolidation , for additional information), the financial results of T2 Entertainment were included in our Consolidated Financial Statements.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Pursuant to various agreements entered into among Shanghai T2 Advertisement Co., Ltd. ( T2 Advertisement ), T2 Technology and the equity interest owners of T2 Advertisement, until June 30, 2010, T2CN, through its wholly owned subsidiary T2 Technology, had effective control over T2 Advertisement and was considered the primary beneficiary of T2 Advertisement. T2 Advertisement was established to hold the necessary licenses required for the operation of our Asian online game related advertisement services in the PRC. Accordingly, from the date that we consolidated T2CN through July 1, 2010, the date we deconsolidated T2CN (See Note 5, Deconsolidation , for additional information), the financial results of T2 Advertisement were included in our Consolidated Financial Statements.

T2 Technology also entered into various agreements with Shanghai Jinyou Network & Technology Co., Ltd. ( Jinyou ) and the equity interest owners of Jinyou. Until June 30, 2010, T2CN, through its wholly owned subsidiary T2 Technology, had effective control over Jinyou and was considered the primary beneficiary of Jinyou. In September 2008, Jinyou acquired an ICP license required for the operation of our Asian online game and services business in the PRC and the agreements entered into by and among T2 Technology, Jinyou and the equity interest owners of Jinyou became effective. Accordingly, the financial results of Jinyou were included in our Consolidated Financial Statements starting from September 2008 through July 1, 2010.

T2 Technology, J-Town Information (Shanghai) Co., Ltd. ( J-Town ), T2 Entertainment, T2 Advertisement and Jinyou are hereby collectively referred to as T2CN Operating Entities .

As a result of a dispute that arose in July 2010 with T2CN 's former Chief Executive Officer, we had been prevented from obtaining the financial information necessary to report the financial results of T2CN, and we had effectively lost control over T2CN 's financial reporting process. Therefore, we deconsolidated T2CN 's financial results with effect from July 1, 2010. As a result, we also ceased treating T2 Entertainment, T2 Advertisement and Jinyou as our variable-interest entities. (See Note 5, Deconsolidation , for additional information.)

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The net assets, total assets and total liabilities in the aggregate of T2 Entertainment, T2 Advertisement and Jinyou were approximately \$2.5 million, \$20.9 million and \$18.4 million, respectively, as of July 1, 2010 (the date of deconsolidation). For the period from January to June 2010, total revenues and net income in the aggregate of T2 Entertainment, T2 Advertisement and Jinyou recorded in our Consolidated Financial Statements were as follows:

| (in US\$ thousands) | 2010      |
|---------------------|-----------|
| Total revenues      | \$ 10,126 |
| Net income          | \$ 834    |

**NOTE 4. ACQUISITIONS****IAHGames**

In July 2010, we began consolidating Infocomm Asia Holdings Pte Ltd. ( IAHGames ), an online game operator, publisher and distributor in Southeast Asia. We acquired IAHGames in order to enhance our position in the online game market in Southeast Asia and strengthen our online entertainment product portfolio. This primary factor among others, contributed to a purchase price in excess of the fair market value of the net tangible assets and intangible assets acquired.

As of December 31, 2011, we owned 5,982,230 Class A preferred shares and 1,208,881 Class B preferred shares of IAHGames, which represented a controlling financial interest of 80 percent of the total outstanding voting rights of IAHGames.



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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In July 2012, we entered into agreements to sell a 60 percent ownership in IAHGames, together with the sale of a 100 percent ownership in Spring Asia Limited ( Spring Asia ), which has a 30 percent interest in Game First International Corporation ( GFI ). We retained a 20 percent ownership in IAHGames. Upon the closing of the agreements, we deconsolidated the results of IAHGames operations and began accounting for our remaining 20 percent interest under the equity method. (See Note 6, Divestitures and Note 29, Subsequent Event , for additional information.)

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The following unaudited pro-forma information presents a summary of the results of operations of our Company for the year ended December 31, 2010 as if we controlled 80 percent of the total outstanding voting rights of IAHGames and consolidated IAHGames as of the beginning of the period presented:

| (in US\$ thousands, except per share figures)        | 2010<br>Unaudited |
|--|-------------------|
| Net revenue  | \$ 69,403         |
| Loss from operations                                 | (50,378)          |
| Net loss   | (1,570)           |
| Net income attributable to GigaMedia                 | 255               |
| Basic earnings per share attributable to GigaMedia   | 0.00              |
| Diluted earnings per share attributable to GigaMedia | 0.00              |

The unaudited pro-forma supplemental information is based on estimates and assumptions, which we believe are reasonable; they are not necessarily indicative of the consolidated financial position or results of operations in future periods or the results that actually would have been realized had we been a consolidated company during all of 2010. The above unaudited pro-forma financial information includes adjustments for the amortization of identified intangible assets with definite lives.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Monsoon**

We, through IAHGAMES, made an equity investment in Monsoon Online Pte Ltd. ( Monsoon ), an operator and distributor of online games in Southeast Asia, in connection with our acquisition of a controlling financial interest in IAHGAMES with effect from July 1, 2010. In connection with a strategic alliance, Monsoon entered into various agreements with a game licensor to distribute selected games in Southeast Asia (collectively referred to as the Distribution Partnership ). Although IAHGAMES owns 100 percent of the common stock of Monsoon, we decided not to consolidate Monsoon at the time of the acquisition as the game licensor had substantive participating rights in Monsoon's business operations pursuant to Monsoon's management agreement. In September 2011, IAHGAMES, Monsoon and the game licensor entered into an agreement whereby all parties agreed to terminate early Monsoon's management agreement and other agreements with the game licensor which had granted the licensor the abovementioned substantive participating rights in connection with Monsoon. The agreement was effective from August 31, 2011. Starting from September 1, 2011, IAHGAMES had effective control over Monsoon and therefore has consolidated Monsoon since that date.

The agreement was effective from the third quarter of 2011. In January 2012, IAHGAMES and Monsoon's commitments under the Distribution Partnership with the game licensor were fully terminated. The execution and closing of this agreement resulted in the following significant financial statement impacts in our Consolidated Financial Statements:

| (in US\$ thousands)                                     | 2011     |
|---|----------|
| Gain on cancellation of warrant liabilities             | \$ 665   |
| Gain on reversal of impairment of prepaid expenses      | 1,347    |
| Recovery of loss on termination of third-party contract | \$ 2,012 |

**NOTE 5. DECONSOLIDATION**

In June 2007, we began consolidating T2CN, an operator and provider of online sports games in the PRC. As of December 31, 2010 and December 13, 2011, we owned 43,633,681 common shares of T2CN, which represented an ownership interest of 67.09 percent of the total outstanding voting rights of T2CN. We disposed of all of our ownership interest in T2CN in December 2011 through sale to a third party.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

As a result of a dispute with T2CN's former Chief Executive Officer arising in July 2010, GigaMedia was prevented from obtaining access to the assets and financial information of the entities held by T2CN. Therefore, we effectively lost control over T2CN's financial reporting process of that time. In spite of owning 67.09 percent of T2CN's common stock, we deconsolidated T2CN's results with effect from July 1, 2010. The following is a breakdown of our retained investment at the date of deconsolidation:

| (in US\$ thousands)                 | Amount        |
|-------------------------------------|---------------|
| Cash                                | \$ 12,903     |
| Other current assets                | 1,266         |
| Fixed assets / non-current assets   | 1,679         |
| Prepaid licensing and royalty       | 5,339         |
| Intangible assets                   | 1,098         |
| <br>Total assets of T2CN            | <br>22,285    |
| Total liabilities of T2CN           | (12,331)      |
| <br>Net equity of T2CN              | <br>9,954     |
| Noncontrolling interest             | (3,276)       |
| Goodwill acquired                   | 17,500        |
| Advances to T2CN Operating Entities | 1,405         |
|                                     | <br>\$ 25,583 |

In connection with our year-end financial reporting process, we were required to perform an impairment analysis for our investment in and advances to T2CN Operating Entities as of December 31, 2010. Given we had been prevented from obtaining the financial information necessary to report the financial results of T2CN, and we had effectively lost control over a majority of T2CN's assets and its financial reporting process, we decided to completely write-off both our Company's investment in and its advances to T2CN Operating Entities in order to properly reflect GigaMedia's financial position as of December 31, 2010. The impairment charges recorded for the investment and the advances in 2010 were approximately \$22.2 million (after removing the other comprehensive income component of equity related to T2CN from our Company's balance sheet) and approximately \$1.4 million, respectively.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

On December 2, 2011, we entered into an agreement with Hornfull Limited, and Hangzhou NewMargin Ventures Co. Ltd. ( Hangzhou NewMargin ) whereby we agreed to sell all of our ownership interest in T2CN to Hornfull Limited, and Hangzhou NewMargin agreed to guarantee the payment and performance of Hornfull Limited under the agreement. On December 14, 2011, the parties completed the sale and purchase of the T2CN shares. Pursuant to the agreement, we sold all of our ownership interest in T2CN to Hornfull Limited in exchange for a cash payment of \$4.7 million, resulting in a gain of \$4.7 million being recorded in 2011. Hornfull Limited also reimbursed us \$790 thousand in cash for legal fees incurred by us in connection with the T2CN dispute.

**NOTE 6. DIVESTITURES**

**IAHGames**

In July 2012, we entered into agreements to sell 100 percent of the shares of Spring Asia, an investment holding company which owns 30 percent of the shares of GFI, to IAHGames, as well as a 60 percent ownership in IAHGames (with a 20 percent ownership of IAHGames retained by us) to IAHGames management and Management Capital International Limited ( MCIL ), a British Virgin Islands company owned by IAHGames management.

In consideration for the sale of IAHGames and Spring Asia, we are to receive \$3 million in cash. The consideration is to be collected in four equal installments, with the first due upon closing, the second due in October 2012, the third due in January 2013 and the fourth due in April 2013. The payments are collateralized by the shares of Spring Asia and are only released from the escrow in proportion to the payment made upon each installment. The first installment of \$750 thousand was received upon the closing on August 15, 2012. However, the buyer has defaulted on the remaining three installments. We have provided IAHGames sufficient payment demand notices, and also granted the buyer a 90-day curing period for each defaulted payment following the due dates for each of the respective installments. Additionally, we have also provided notices upon the expiration of each of the 90-day curing period of our intention to enforce repossession rights on the proportionate shares held by the escrow agent. The curing period of the last installment will expire on July 2, 2013. (See Note 29, Subsequent Event , for additional information.)

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Our Company accounted for the deconsolidation of and the retained noncontrolling investment in IAHGames in August 2012 at fair value. Considering the uncertainty as to the collectability of the remaining three installments, we deferred the disposal gain of \$211 thousand against the consideration installments receivable of \$2,250 thousand as of December 31, 2012. The deferred gain is measured as the difference between:

| (In US\$ thousand)  | Amount   |
|---|----------|
| The fair value of consideration received and receivable, net of any transaction costs, plus           | \$ 3,000 |
| The fair value of the 20% retained noncontrolling investment in IAH at the date of deconsolidation    |          |
|   | 3,000    |
| The carrying amount (credit balance) of IAHGames at the date of deconsolidation                       | (14,536) |
| Net receivables due to GigaMedia from IAHGames waived upon the closing of the sale                    | 17,542   |
| Other comprehensive income component of equity related to IAHGames at the date of the deconsolidation | (217)    |
|   | 2,789    |
| Deferred gain on deconsolidation of IAH   | \$ 211   |

JIDI Network Technology (Shanghai) Co., Ltd. ( JIDI )

In June 2012, our board of directors approved a plan to liquidate and dissolve JIDI, a wholly-owned subsidiary, and Shanghai JIDI, a VIE controlled through a series of contractual arrangements.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Results for JIDI and Shanghai JIDI operations are reported as discontinued operations for all periods presented. The carrying amounts of the remaining assets and liabilities of JIDI and Shanghai JIDI were not significant to our Consolidated Financial Statements as of December 31, 2012, and we recorded a loss of approximately \$588 thousand in connection with the disposal of property, plant and equipment, which is included within discontinued operations. Summarized selected financial information for discontinued operations of JIDI and Shanghai JIDI are as follows:

| (in US\$ thousands)                          | 2011       | 2012       |
|--|------------|------------|
| Revenue                                      | \$ 29      | \$ 100     |
| Loss from discontinued operations before tax | \$ (4,240) | \$ (2,521) |
| Income tax expense                           |            |            |
| Loss from discontinued operations            | \$ (4,240) | \$ (2,521) |

**Gaming software and service business**

On December 15, 2009, we entered into an agreement with BEG to sell 60 percent of substantially all of the assets and liabilities of our gaming software and service business for approximately \$100 million in cash, subject to certain adjustments. The closing of the sale occurred on April 8, 2010. The sale resulted in the recognition of a gain of \$79.1 million, net of transaction costs. The sale of the remaining 40 percent was subject to a put and call mechanism in place between GigaMedia and BEG, as defined in the agreement. GigaMedia had the option to put all or part of its remaining 40 percent to BEG in each of 2013, 2014, and 2015 at a value considering all relevant facts and circumstances after the end of each year. If the put option owned by GigaMedia was not fully exercised, BEG would have the option to call the remaining interest held by GigaMedia in each of 2015 and 2016.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

We deconsolidated the gaming software and service business and recognized a gain when we completed the sale of 60 percent of substantially all of the assets and liabilities to BEG on April 8, 2010, the date on which our Company ceased to have a controlling financial interest. The remaining ownership we retained in the gaming software and service business, a 40 percent, later diluted to 33.66 percent interest had been accounted for under the equity method accounting from April 2010 to July 2012, when we entered into another agreement with BEG to sell our remaining ownership interest in the gaming software and service business for a consideration of \$1.7 million. Of this consideration, \$985 thousand was paid to us in cash, while the remainder related to the extinguishment of a 2009 tax liability. The closing of the sale occurred in August 2012. The sale resulted in the recognition of a gain of \$2.5 million, net of transaction costs.

Our Company accounted for the deconsolidation of the gaming software and service business in 2010 at fair value and recognized a gain of \$79.1 million measured as the difference between:

| (In US\$ thousands)  | 2010      |
|--|-----------|
| The fair value of any consideration received, including purchase price adjustments, net of any transaction costs                                     | \$ 82,984 |
| The fair value of the 40% retained noncontrolling investment in the gaming software and service business at the date the business was deconsolidated | 54,240    |
| Less : The carrying amount of the gaming software and service business at the date of the deconsolidation  | (58,084)  |
| Gain on deconsolidation of the gaming software and services business   | \$ 79,140 |



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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 7. GOODWILL**

The following table summarizes the changes to our Company's goodwill:

| (In US\$ thousands)   | 2010      | 2011      | 2012      |
|---|-----------|-----------|-----------|
| Balance at beginning of year  | \$ 44,417 | \$ 39,493 | \$ 28,437 |
| Acquisition - IAHGames (Note 4) and OneNet                                    | 12,188    | 1,049     |           |
| Impairment charge - T2CN, IAHGames, OneNet and FunTown (Notes 5 and 10)       | (19,755)  | (5,097)   | (12,489)  |
| Reversal of contingent payment of minimum guarantee under licensing agreement |           | (5,885)   |           |
| Translation adjustment  | 2,643     | (1,123)   | 986       |
| Balance at end of year  | \$ 39,493 | \$ 28,437 | \$ 16,934 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 8. INTANGIBLE ASSETS - NET**

The following table summarizes our Company's intangible assets, by major asset class:

| (In US\$ thousands)                              | December 31, 2012     |                          |           |
|--|-----------------------|--------------------------|-----------|
|  | Gross carrying amount | Accumulated amortization | Net       |
| <b><u>Finite-lived intangible assets</u></b>     |                       |                          |           |
| Completed technology                             | \$ 2,603              | \$ 2,603                 | \$        |
| Capitalized software development cost            | 3,480                 | 1,414                    | 2,066     |
| Customer relationships                           | 6,274                 | 4,880                    | 1,394     |
| Other  | 137                   | 133                      | 4         |
|  | 12,494                | 9,030                    | 3,464     |
| <b><u>Indefinite-lived intangible assets</u></b> |                       |                          |           |
| Trade name and trademark                         | 12,211                |                          | 12,211    |
|  | \$ 24,705             | \$ 9,030                 | \$ 15,675 |

| (In US\$ thousands)                              | December 31, 2011     |                          |           |
|--|-----------------------|--------------------------|-----------|
|  | Gross carrying amount | Accumulated amortization | Net       |
| <b><u>Finite-lived intangible assets</u></b>     |                       |                          |           |
| Completed technology                             | \$ 2,497              | \$ 2,140                 | \$ 357    |
| Capitalized software development cost            | 7,525                 | 6,112                    | 1,413     |
| Customer relationships                           | 6,017                 | 4,011                    | 2,006     |
| Other  | 206                   | 159                      | 47        |
|  | 16,245                | 12,422                   | 3,823     |
| <b><u>Indefinite-lived intangible assets</u></b> |                       |                          |           |
| Trade name and trademark                         | 11,711                |                          | 11,711    |
|  | \$ 27,956             | \$ 12,422                | \$ 15,534 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The finite-lived intangible assets are amortized over their estimated useful lives ranging from 3 to 9 years, with the overall weighted-average life of 5.5 years.

For the years ended December 31, 2010, 2011 and 2012, total amortization expense of intangible assets were \$2.7 million, \$2.3 million and \$2.2 million, respectively, which includes amortization of capitalized software development costs of \$1.5 million, \$962 thousand and \$1.1 million. As of December 31, 2012, based on the current amount of intangibles subject to amortization, the estimated amortization expense for each of the following years is as follows:

| (In US\$ thousands) | Amount   |
|---------------------|----------|
| 2013                | \$ 1,389 |
| 2014                | 1,386    |
| 2015                | 689      |
|                     | \$ 3,464 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 9. PREPAID LICENSING AND ROYALTY FEES**

The following table summarizes changes to our Company's prepaid licensing and royalty fees:

| (in US\$ thousands)  | 2010     | 2011     | 2012     |
|--|----------|----------|----------|
| Balance at beginning of year   | \$ 5,557 | \$ 4,214 | \$ 7,103 |
| Net operating additions  | 3,855    | 3,379    | 2,395    |
| Acquisition - IAHGames and OneNet  | 1,011    | 129      |          |
| Deconsolidation (Note 5) - T2CN and IAHGames                               | (5,339)  |          | (152)    |
| Impairment charges (Note 10)   | (870)    | (247)    | (702)    |
| Impairment charges (Note 10) recorded in loss from discontinued operations |          | (372)    |          |
| Balance at end of year   | \$ 4,214 | \$ 7,103 | \$ 8,644 |

**NOTE 10. FAIR VALUE MEASUREMENTS**

The accounting framework for determining fair value includes a hierarchy for ranking the quality and reliability of the information used to measure fair value, which enables the reader of the financial statements to assess the inputs used to develop those measurements. The fair value hierarchy consists of three tiers as follows: Level 1, defined as quoted market prices in active markets for identical assets or liabilities; Level 2, defined as inputs other than Level 1 that are observable, either directly or indirectly, such as quoted market prices for similar assets or liabilities, quoted prices in markets that are not active, model-based valuation techniques for which all significant assumptions are observable in the market, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets and liabilities; and Level 3, defined as unobservable inputs that are not corroborated by market data.

***Assets and Liabilities that are Measured at Fair Value on a Recurring Basis***

Our Company has segregated all financial assets and liabilities that are measured at fair value on a recurring basis (at least annually) into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date in the table below.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Assets and liabilities measured at fair value on a recurring basis are summarized as below:

| (in US\$ thousands)                | Fair Value Measurement Using |          |          | Year Ended<br>December 31,<br>2012 |
|------------------------------------|------------------------------|----------|----------|------------------------------------|
|                                    | Level 1                      | Level 2  | Level 3  |                                    |
| <b>Assets</b>                      |                              |          |          |                                    |
| Cash equivalents - time deposits   | \$                           | \$ 1,514 | \$       | \$ 1,514                           |
| Marketable securities - current    |                              |          |          |                                    |
| Equity securities                  | 17,773                       |          |          | 17,773                             |
| Marketable securities - noncurrent |                              |          |          |                                    |
| Debt securities                    |                              |          | 2,727    | 2,727                              |
| Equity securities                  |                              |          | 1,565    | 1,565                              |
|                                    | \$ 17,773                    | \$ 1,514 | \$ 4,292 | \$ 23,579                          |

| (in US\$ thousands)                | Fair Value Measurement Using |          |          | Year Ended<br>December 31,<br>2011 |
|------------------------------------|------------------------------|----------|----------|------------------------------------|
|                                    | Level 1                      | Level 2  | Level 3  |                                    |
| <b>Assets</b>                      |                              |          |          |                                    |
| Cash equivalents - time deposits   | \$                           | \$ 6,631 | \$       | \$ 6,631                           |
| Marketable securities - current    |                              |          |          |                                    |
| Equity securities                  | 42,347                       |          |          | 42,347                             |
| Marketable securities - noncurrent |                              |          |          |                                    |
| Debt securities                    |                              |          | 5,454    | 5,454                              |
| Equity securities                  |                              | 1,630    |          | 1,630                              |
|                                    | \$ 42,347                    | \$ 8,261 | \$ 5,454 | \$ 56,062                          |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Level 1 and 2 measurements:**

Cash equivalents time deposits are convertible into a known amount of cash and are subject to an insignificant risk of change in value. Certain marketable securities are valued using a market approach based on the quoted market prices of identical instruments when available, or other observable inputs such as trading prices of identical instruments in inactive markets. The fair value of the marketable equity securities that have publicly quoted trading prices are valued using those observable prices, unless adjustments are required to available observable inputs.

In 2010, 2011 and 2012, we recorded unrealized gains (losses) of \$21.8 million, \$16.2 million and \$(24.0) million, respectively, on marketable securities, which are included in other comprehensive income

**Level 3 measurements:**

For assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during 2011 and 2012, a reconciliation of the beginning and ending balances are presented as follows:

| (in US\$ thousands)   | Marketable Securities -<br>Debt<br>and Equity Securities |          |
|---|--|----------|
|   | 2011   | 2012     |
| Balance at beginning of year  | \$ 5,454   | \$ 5,454 |
| Total gains or (losses) (realized/unrealized) included in earnings  |  | (493)    |
| Purchase  |  |          |
| Sale  |  | (2,727)  |
| Transfer into Level 3   |  | 2,058    |
| Balance at end of year  | \$ 5,454   | \$ 4,292 |
| The amount of total gains or (losses) for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at the reporting date. | \$   | \$ 493   |

The fair values of the marketable debt and equity securities are derived using a discounted cash flow method using unobservable inputs. The discounted cash flow method incorporates adjusted available market discount rate information and our Company's estimates of liquidity risk, and other cash flow model related assumptions.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In 2010, 2011 and 2012, we recognized other-than-temporary impairments of \$4.5 million, \$0 and \$493 thousand, respectively, related to marketable debt and equity securities, which is included in non-operating expenses within impairment loss on marketable securities and investments in the Consolidated Statements of Income (Loss).

For liabilities measured at fair value on a recurring basis using significant unobservable inputs (level 3) during 2011, a reconciliation of the beginning and ending balances are presented as follows (there were none during 2012):

| (in US\$ thousands)  | Other liabilities<br>- Warrant<br>Derivative<br>2011 |
|--|--|
| Balance at beginning of year   | \$ 665   |
| Total (gains) or losses (realized/unrealized) included in earnings   | (665)  |
| Purchase   |  |
| Balance at end of year   | \$   |
| The amount of total (gains) or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to liabilities still held at the reporting date. | \$   |

IAHGames had warrants outstanding in which the holder could purchase an aggregate of 15 percent of IAHGames common stock, on a fully diluted basis, at an exercise price of \$3.40 per warrant share subject GigaMedia's share of loss to certain adjustments in accordance with the warrant agreement. The warrants expired upon the expiration of certain game licenses or in certain circumstances in accordance with the warrant agreement.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In 2010, we recognized a gain of approximately \$2.6 million related to the revaluation of the warrants, which is included in non-operating income (expenses) within gain on fair value changes of warrant derivative in the Consolidated Statements of Income (Loss).

As a part of the early termination of the management agreement related to Monsoon (please refer to Note 4, Acquisition ), all the warrants outstanding were cancelled. As a result, we recognized a gain of \$665 thousand upon cancellation of the warrants in 2011.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Financial instruments:**

The carrying amounts of our Company's cash, accounts receivable, restricted cash, accounts payable, and short-term debt approximate fair value due to their short-term maturities. The fair value of amounts due to and from related parties is not practicable to estimate due to the related party nature of the underlying transactions.

**Assets and Liabilities that are Measured at Fair Value on a Nonrecurring Basis**

Assets and liabilities measured at fair value on a nonrecurring basis include measuring impairment when required for long-lived assets. For GigaMedia, long-lived assets measured at fair value on a nonrecurring basis include investments accounted for under the equity method and cost method, property, plant, and equipment, intangible assets, prepaid licensing and royalty fees, and goodwill.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Assets and liabilities measured at fair value on a nonrecurring basis that were determined to be impaired as of December 31, 2011 and 2012 are summarized as below:

| (in US\$ thousands)                                  | Fair Value measurement Using |            |                  | Year Ended<br>December 31,<br>2012 | Total<br>Impairment<br>Losses |
|--|------------------------------|------------|------------------|------------------------------------|-------------------------------|
|  | Level<br>1                   | Level<br>2 | Level 3          |                                    |                               |
| Assets   |                              |            |                  |                                    |                               |
| (a) Investments - Cost-method                        | \$                           | \$         | \$               | \$                                 | \$ 700                        |
| (b) Goodwill - Resulting from acquisition of FunTown |                              |            | 16,934           | 16,934                             | 12,489                        |
| (c) Intangible assets - Capitalized software cost    |                              |            |                  |                                    | 15                            |
| (d) Prepaid licensing and royalty fees               |                              |            |                  |                                    | 702                           |
| <b>Total</b>   | <b>\$</b>                    | <b>\$</b>  | <b>\$ 16,934</b> | <b>\$ 16,934</b>                   | <b>\$ 13,906</b>              |

| (in US\$ thousands)   | Fair Value measurement Using |           |                 | Year Ended<br>December 31,<br>2011 | Total<br>Impairment<br>Losses |
|---|------------------------------|-----------|-----------------|------------------------------------|-------------------------------|
|   | Level 1                      | Level 2   | Level 3         |                                    |                               |
| Assets  |                              |           |                 |                                    |                               |
| (a) Investments - Cost-method                               | \$                           | \$        | \$ 700          | \$ 700                             | \$ 679                        |
| (a) Investments - Equity-method                             |                              |           | 2,500           | 2,500                              | 12,648                        |
| (b) Goodwill - Resulting from acquisition of IAH and OneNet |                              |           |                 |                                    | 5,097                         |
| (c) Intangible assets - Capitalized software cost           |                              |           |                 |                                    | 40                            |
| (c) Intangible assets - Favorable lease right               |                              |           |                 |                                    | 2,543                         |
| (d) Prepaid licensing and royalty fees                      |                              |           |                 |                                    | 619                           |
| <b>Total</b>  | <b>\$</b>                    | <b>\$</b> | <b>\$ 3,200</b> | <b>\$ 3,200</b>                    | <b>\$ 21,626</b>              |

(a) Impairment losses on certain cost method and equity method investments which were determined to be impaired:

In 2011, certain cost method investments with carrying amounts of \$1.4 million were written down to their estimated fair value of \$700 thousand, resulting in an impairment charge of \$679 thousand, and an equity method investment with a carrying amount of \$15.1 million was written down to its estimated fair value of \$2.5 million, resulting in an impairment charge of \$12.6 million. In 2012, certain cost method investments were fully written down, resulting in an impairment charge of \$700 thousand. The impairment charges are included in non-operating expenses within impairment loss on marketable securities and investments in the Consolidated Statements of Income (Loss).

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Cost method and equity method investments are measured at fair value on a nonrecurring basis when declines in fair value are determined to be other-than-temporary, using other observable inputs such as trading prices of similar classes of the stock or using discounted cash flows, incorporating adjusted available market discount rate information and our Company's estimates for liquidity risk.

(b) Impairment losses on goodwill which was determined to be impaired:

Goodwill from the acquisition of FunTown, which constitutes our Asian online game and service business, was written down to its estimated fair value of \$16.9 million as of December 31, 2012, resulting in an impairment charge of \$12.5 million in the fourth quarter 2012, which is included within operating expenses in the Consolidated Statements of Income (Loss). As a result of the slowdown in the PC-based online game market and our repositioning of FunTown to focus on market growth in browser/mobile games in the multi-platform market, we estimated that the fair value of our Asian online game and service business had decreased and, as a result, impaired the goodwill related to FunTown as of December 31, 2012. The impairment charge was determined by our estimates of future cash flows from the FunTown business which have been reduced due our change in strategic focus to self-developed casual games versus licensed MMOs (massive multiplayer online games) and the slowdown in the PC-based online games market where we are currently positioned, indicating that the original carrying amount of the goodwill from the acquisition of FunTown could not be fully recovered as of December 31, 2012.

Goodwill from the acquisition of IAHGames was fully written down to \$0 as of December 31, 2011, resulting in an impairment charge of \$4.0 million in 2011, which is included within operating expenses in the Consolidated Statements of Income (Loss). The impairment charges resulted as our estimates of future cash flows for IAHGames' business had been reduced due to lower than expected operating performance results in 2011, indicating that the carrying amount of the goodwill from the acquisition of IAHGames could not be fully recovered as of December 31, 2011.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Goodwill from the acquisition of OneNet Co., Ltd. ( OneNet ) was fully written down to \$0 as of December 31, 2011, resulting in an impairment charge of \$1.0 million in 2011, which is included within operating expenses in the Consolidated Statements of Income (Loss). The impairment charge resulted as our estimates of future cash flows for OneNet s business had been reduced due to lower than expected operating performance results in 2011, indicating that the carrying amount of the goodwill from the acquisition of OneNet could not be fully recovered as of December 31, 2011.

Goodwill is valued on a nonrecurring basis when impairment exists, using unobservable inputs such as discounted cash flows, incorporating adjusted available market discount rate information and our Company s estimates for liquidity risk and other cash flow model related assumptions.

(c) Impairment losses on certain intangible assets which were determined to be impaired:

In 2011 and 2012, certain capitalized software development costs were fully written down, resulting in impairment charges of \$40 thousand and \$15 thousand, respectively, included in operating expenses within impairment loss on intangible assets in the Consolidated Statements of Income (Loss). The impairment charges for the capitalized software costs were the result of certain projects within our Asian online game and service business that we ceased further development on, and as a result, we recorded a full impairment of the carrying value of the assets related to these projects.

As of December 31, 2011, a favorable lease right resulting from the acquisition of IAHGames with a carrying amount of \$2.5 million was fully written down, resulting in an impairment charge of \$2.5 million. This impairment is included in operating expenses within impairment loss on intangible assets in the Consolidated Statements of Income (Loss). The impairment charges resulted as our estimates of future cash flows related to the favorable lease right were reduced to lower than originally expected, which indicated that the carrying amount of these intangible assets could not be recovered as of December 31, 2011.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

(d) Impairment losses on certain prepaid licensing and royalty fees which were determined to be impaired:

In 2011 and 2012, certain prepaid licensing and royalty fees were fully written down, resulting in impairment charges of \$619 and \$702 thousand, respectively. This impairment is included in operating expenses in the Consolidated Statements of Income (Loss). The impairment charges for the prepaid licensing and royalty fees related to certain licensed games within our Asian online game and service business that we stopped operating or for which the carrying amounts of the related assets were determined not to be recoverable from their expected future undiscounted cash flows. The licensing fee games and related royalties are valued on a nonrecurring basis when impairment exists, using unobservable inputs such as discounted cash flows, incorporating adjusted available market discount rate information and our Company's estimates for liquidity risk, along with other cash flow model related assumptions.

**NOTE 11. CASH AND CASH EQUIVALENTS**

Cash and cash equivalents consist of the following:

| (in US\$ thousands)       | December 31 |           |
|---------------------------|-------------|-----------|
|                           | 2011        | 2012      |
| Cash and savings accounts | \$ 57,366   | \$ 61,217 |
| Time deposits             | 6,631       | 1,514     |
|                           | \$ 63,997   | \$ 62,731 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

We maintain cash and cash equivalents in bank accounts with major financial institutions with high credit ratings located in the following jurisdictions:

| (in US\$ thousands) | December 31 |           |
|---------------------|-------------|-----------|
|                     | 2011        | 2012      |
| Taiwan              | \$ 45,098   | \$ 59,195 |
| Hong Kong           | 4,467       | 2,809     |
| PRC                 | 6,759       | 626       |
| Malaysia            | 100         | 100       |
| Korea               | 6,260       |           |
| Singapore           | 1,105       |           |
| Thailand            | 113         |           |
| Others              | 95          | 1         |
|                     | \$ 63,997   | \$ 62,731 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 12. MARKETABLE SECURITIES - CURRENT**

Marketable securities - current consist of the following:

| (in US\$ thousands)            | December 31 |           |
|--------------------------------|-------------|-----------|
|                                | 2011        | 2012      |
| Available-for-sale securities: |             |           |
| Equity securities              | \$ 42,347   | \$ 17,773 |

All of our Company's marketable securities - current are classified as available-for-sale. As of December 31, 2011 and 2012, the balances of unrealized gains for marketable securities - current were \$38.8 million and \$14.4 million, respectively. During 2010, 2011 and 2012, realized gains from the disposal of marketable securities - current amounted to \$0, \$535 thousand, and \$2.3 million, respectively. The costs for calculating gains on disposal were based on each security's average cost.

**NOTE 13. ACCOUNTS RECEIVABLE - NET**

Accounts receivable consist of the following:

| (in US\$ thousands)                   | December 31 |          |
|---------------------------------------|-------------|----------|
|                                       | 2011        | 2012     |
| Accounts receivable                   | \$ 9,045    | \$ 2,959 |
| Less: Allowance for doubtful accounts | (2,594)     | (130)    |
|                                       | \$ 6,451    | \$ 2,829 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The following is a reconciliation of changes in our Company's allowance for doubtful accounts during the years ended December 31, 2010, 2011 and 2012:

| (in US\$ thousands)                       | 2010   | 2011     | 2012     |
|---|--------|----------|----------|
| Balance at beginning of year              | \$ 200 | \$ 842   | \$ 2,594 |
| Additions: Provision for bad debt expense | 156    | 1,820    | 169      |
| Less: Write-offs                          | (219)  | (61)     | (269)    |
| Acquisition - IAHHGames                   | 691    |          |          |
| Deconsolidation - IAHHGames               |        |          | (2,370)  |
| Translation adjustment                    | 14     | (7)      | 6        |
| Balance at end of year                    | \$ 842 | \$ 2,594 | \$ 130   |

**NOTE 14. OTHER CURRENT ASSETS**

Other current assets consist of the following:

| (in US\$ thousands)                                 | December 31 |          |
|---|-------------|----------|
|   | 2011        | 2012     |
| Loans receivable - current                          | \$ 5,666    | \$ 3,437 |
| Less: Allowance for loans receivable - current      | (5,057)     | (3,437)  |
| Deferred income tax assets - current, net (Note 25) | 759         | 840      |
| Other   | 183         | 161      |
|   | \$ 1,551    | \$ 1,001 |

The following is a reconciliation of changes in our Company's allowance for loans receivable - current during the years ended December 31, 2010, 2011 and 2012:

| (in US\$ thousands)                        | 2010     | 2011     | 2012     |
|--|----------|----------|----------|
| Balance at beginning of year               | \$ 3,574 | \$ 5,057 | \$ 5,057 |
| Additions: Provision for bad debt expenses | 1,483    |          |          |
| Less: Write-offs                           |          |          | (1,620)  |
| Balance at end of year                     | \$ 5,057 | \$ 5,057 | \$ 3,437 |



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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

As of the date of our deconsolidation of T2CN in July 2010, we had \$1.4 million of loans receivable outstanding. As a result of the ongoing dispute, we do not expect to collect these outstanding loans due from T2CN. Therefore, we recognized a full provision for the loans of \$1.4 million in 2010. (See Note 5, Deconsolidation for additional information.)

**NOTE 15. MARKETABLE SECURITIES - NONCURRENT**

Marketable securities - noncurrent consist of the following:

| (in US\$ thousands)           | December 31 |          |
|-------------------------------|-------------|----------|
|                               | 2011        | 2012     |
| Available-for-sale securities |             |          |
| Debt securities               | \$ 5,454    | \$ 2,727 |
| Equity securities             | 1,630       | 1,565    |
|                               | \$ 7,084    | \$ 4,292 |

Our Company's marketable securities - noncurrent are invested in convertible preferred shares and publicly-traded common shares and are classified as available-for-sale securities.

The preferred shares are convertible into common shares on 1:1 basis, subject to certain adjustments, and shall be automatically converted upon certain conditions outlined in the agreements. The convertible preferred shares are all redeemable based upon certain agreed-upon conditions.

The embedded conversion options of the convertible preferred shares do not meet the definition of derivative instruments defined in the FASB accounting standards codification and therefore are not bifurcated from the preferred share investment.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

We have also considered and determined whether our investments in preferred shares are in-substance common shares which should be accounted for under the equity method. Given that our convertible preferred shares have substantive redemption rights and thus do not meet the criteria of in-substance common shares, we have accounted for them as debt securities in accordance with the guidance issued by FASB Accounting Standards Codification.

During 2010, 2011 and 2012, realized gains from the disposal of marketable securities – non-current amounted to \$0, \$5.8 million and \$3.4 million, respectively. Gains on disposal were based on the security's average cost. In December 2011, our Board of Directors authorized management to dispose of a majority of our equity securities in the first half of 2012. Accordingly, we reclassified those marketable securities as current as of December 31, 2011. In 2012 we disposed of 74 thousand shares, or 6.07 percent, of such marketable securities (valued at \$2.5 million as of the time of sale) with realized gains of \$2.3 million. Due to the downturn in global economy and the securities market in 2012, all of the sales were not completed, and therefore were re-authorized to proceed in 2013. (See Note 12, Marketable Securities – Current, for additional information.)

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 16. INVESTMENTS**

Investments consist of the following:

| (in US\$ thousands)                               | December 31 |          |
|---|-------------|----------|
|   | 2011        | 2012     |
| Investments accounted for under the equity method | \$ 7,615    | \$ 5,223 |
| Investments accounted for under the cost method   | 700         |          |
|   | \$ 8,315    | \$ 5,223 |

Our Company's investments in companies that are accounted for under the equity method of accounting primarily consist of the following: (a) through July 31, 2012, a 40 percent, later diluted to 33.66 percent interest in Mangas Everest S.A.S. (Mangas Everest), which is engaged in the gaming software and service business (See Note 6 Divestitures for additional information); (b) through August 15, 2012, a 30 percent interest in Game First International Corporation (GFI), an operator and distributor of online games in Taiwan (See Note 6 Divestitures for additional information); (c) through August 31, 2011, a 100 percent interest in Monsoon Online Pte Ltd. (Monsoon), an operator and distributor of online games in Southeast Asia; and (d) an 18 percent interest in East Gate Media Contents & Technology Fund (East Gate), a Korean Fund that invests in online game businesses and films. The investments in these companies amounted to \$7.6 million and \$5.2 million as of December 31, 2011 and 2012, respectively.

As of December 31, 2011, our share of the underlying net assets of Mangas Everest exceeded the carrying value of its investment by \$9.3 million. The excess results from the difference between the fair value we assigned to the 40 percent retained interest in Mangas Everest at the date the business was deconsolidated, compared to 40 percent of the total fair value of Mangas Everest as determined by BEG, the purchaser of the 60 percent interest.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

From the date of our sale of a 60 percent interest in our online gaming software and service business in 2010 through July 31, 2012 when we sold the remaining 33.66 percent interest to BEG, we recognized our share of losses in Mangas Everest under the equity method of accounting which totaled \$9.8 million, \$49.7 million and \$0 in 2010, 2011 and 2012, respectively, which resulted in a negative investment balance as of December 31, 2011 and July 31, 2012. In accordance with the FASB codification, we charged this negative investment balance against the loan receivable that Mangas Everest had outstanding to us as of December 31, 2011 and July 31, 2012. (See Note 26, Related Party Transactions , for additional information.)

We, through IAHGames, made an equity investment in Monsoon in connection with our acquisition of a controlling financial interest in IAHGames. Although IAHGames owns 100 percent of the common stock of Monsoon, prior to September 2011 we determined that Monsoon could not be consolidated by IAHGames due to the substantive participating rights that the game licensor had in Monsoon pursuant to Monsoon's management agreement. From the date of our acquisition of IAHGames through August 31, 2011, we recognized our share of gains (losses) under the equity method of accounting which totaled \$(12.6) million and \$230 thousand in 2010 and 2011, respectively, which resulted in a negative investment balance. In accordance with the FASB codification, we charged this negative investment balance against the loan receivable that Monsoon had outstanding to us as of December 31, 2010 and August 31, 2011. (See Note 26, Related Party Transactions , for additional information.)

In September 2011, IAHGames, Monsoon and the game licensor entered a transition agreement to early terminate the previous agreement in which the abovementioned substantive participating rights were granted, effective August 31, 2011, and thus restored IAHGames' full control in Monsoon. Therefore, starting September 1, 2011, we consolidated Monsoon. (See Note 4, Acquisition , for additional information.)

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Our Company has an 18 percent interest in East Gate, a Korean Limited Partnership. We account for this limited partnership investment under the equity method accounting in accordance with the FASB codification as our interest is not considered to be minor. We have influence over partnership operating and financial policies based on the terms of the partnership agreement.

**NOTE 17. SHORT-TERM BORROWINGS**

As of December 31, 2011 and 2012, short-term borrowings totaled \$11.8 million and \$7.7 million, respectively. These amounts were borrowed from certain financial institutions. The annual interest rates on these borrowings ranged from 1.30 percent to 7.54 percent for 2011, and was 1.42 percent for 2012. The maturity dates fell in late January 2012 as of December 31, 2011 and in mid-January 2013 as of December 31, 2012. As of December 31, 2011 and 2012, the weighted-average interest rate on total short-term borrowings was 2.87 percent and 1.42 percent, respectively.

As of December 31, 2012, the total amount of unused lines of credit available for borrowing under these agreements was approximately \$6.9 million.

During the period from January 2013 to March 2013, we repaid certain short-term borrowings totaling \$22.9 million, and renewed short-term borrowing agreements totaling \$22.9 million.

We pledged certain time deposits, land, and buildings as collateral for borrowings from certain financial institutions. The total value of collateral amounted to \$4.2 million and \$0 as of December 31, 2011 and 2012, respectively, in which time deposits pledged are recorded as restricted cash totaling \$3 million and \$0 as of December 31, 2011 and 2012, respectively.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 18. ACCRUED EXPENSES**

Accrued expenses consist of the following:

| (in US\$ thousands)                      | December 31 |          |
|--|-------------|----------|
|  | 2011        | 2012     |
| Accrued advertising expenses             | \$ 717      | \$ 696   |
| Accrued royalties                        | 1,269       | 967      |
| Accrued professional fees                | 3,263       | 1,319    |
| Purchase price adjustment accrual to BEG | 2,326       |          |
| Other                                    | 3,059       | 2,200    |
|  | \$ 10,634   | \$ 5,182 |

**NOTE 19. OTHER CURRENT LIABILITIES**

Other current liabilities consist of the following:

| (in US\$ thousands)  | December 31 |          |
|----------------------|-------------|----------|
|                      | 2011        | 2012     |
| Deferred revenue     | \$ 4,319    | \$ 3,174 |
| Income taxes payable | 4,251       | 3,588    |
| Other                | 749         | 398      |
|                      | \$ 9,319    | \$ 7,160 |

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 20. PENSION BENEFITS**

Our Company and our subsidiaries have defined benefit and defined contribution pension plans that cover substantially all of our employees.

***Defined Benefit Pension Plan***

We have a defined benefit pension plan in accordance with the Labor Standards Law of the Republic of China (R.O.C.) for our employees located in Taiwan, covering substantially all full-time employees for services provided prior to July 1, 2005, and employees who have elected to remain in the defined benefit pension plan subsequent to the enactment of the Labor Pension Act on July 1, 2005. Under the defined benefit pension plan, employees are entitled to a lump sum retirement benefit upon retirement equivalent to the aggregate of 2 months pensionable salary for each of the first 15 years of service and 1 month's pensionable salary for each year of service thereafter subject to a maximum of 45 months pensionable salary. The pensionable salary is the monthly average salary or wage of the final six months prior to approved retirement.

We use a December 31 measurement date for our defined benefit pension plan. As of December 31, 2011 and 2012, the accumulated benefit obligation amounted to \$169 thousand and \$429 thousand, respectively, and the funded status of accrued pension liability (prepaid pension) amounted to \$(68) thousand (recorded in other long-term assets for \$239 thousand and accrued pension liabilities for \$171 thousand) and \$281 thousand, respectively. The fair value of plan assets amounted to \$263 thousand and \$291 thousand as of December 31, 2011 and 2012, respectively. The accumulated other comprehensive income amounted to \$308 thousand and \$2 thousand as of December 31, 2011 and 2012, respectively. The net periodic benefit cost (income) for 2010, 2011 and 2012 amounted to \$12 thousand, \$(18) thousand and \$30 thousand, respectively.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

We have contributed an amount equal to 2 percent of the salaries and wages paid to all qualified employees located in Taiwan to a pension fund (the Fund). The Fund is administered by a pension fund monitoring committee (the Committee) and deposited in the Committee's name in the Bank of Taiwan. Our Company makes pension payments from our account in the Fund unless the Fund is insufficient, in which case we make payments from internal funds as payments become due. We seek to maintain a normal, highly liquid working capital balance to ensure payments are made timely.

We expect to make a contribution of \$8 thousand to the Fund in 2013. We do not expect to make any benefit payments through 2020.

***Defined Contribution Pension Plans***

We have provided defined contribution plans for employees located in Taiwan, the PRC, Hong Kong and Singapore. Contributions to the plans are expensed as incurred.

**Taiwan**

Pursuant to the new Labor Pension Act enacted on July 1, 2005, our Company has a defined contribution pension plan for our employees located in Taiwan. For eligible employees who elect to participate in the defined contribution pension plan, we contribute no less than 6 percent of an employee's monthly salary and wage and up to the maximum amount of NT\$9 thousand (approximately \$310), to each of the eligible employees' individual pension accounts at the Bureau of Labor Insurance each month. Pension payments to employees are made either by monthly installments or in a lump sum from the accumulated contributions and earnings in employees' individual accounts.

**PRC**

All PRC employees participate in employee social security plans, including pension and other welfare benefits, which are organized and administered by governmental authorities. We have no other substantial commitments to employees. The premiums and welfare benefit contributions that should be borne by our Company are calculated in accordance with relevant PRC regulations, and are paid to the labor and social welfare authorities.



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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Hong Kong**

According to the relevant Hong Kong regulations, we provide a contribution plan for the eligible employees in Hong Kong. We must contribute at least 5 percent of the employees' total salaries. For this purpose, the monthly relevant contribution to their individual contribution accounts is subject to a cap of HK\$1.25 thousand (approximately \$161). After the termination of employment, the benefits still belong to the employees in any circumstances.

**Singapore**

In accordance with Singapore regulations, through July 2012 we made contributions to the Singapore Central Provident Fund Scheme, a defined contribution pension plan, for eligible employees. We contributed 14.5 percent of the employees' gross salaries, subject to a cap of SG\$5 thousand (approximately \$4,000). We have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and preceding financial years.

The total amount of defined contribution pension expenses pursuant to our defined contribution plans for the years ended December 31, 2010, 2011, and 2012 were \$1.0 million, \$896 thousand, and \$585 thousand, respectively.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 21. OTHER LIABILITIES - OTHER**

Other liabilities consist of the following:

| (in US\$ thousands)                | December 31 |        |
|------------------------------------|-------------|--------|
|                                    | 2011        | 2012   |
| Deferred tax liabilities (Note 25) | \$ 1,006    | \$ 561 |
| Other                              | 9           | 12     |
|                                    | \$ 1,015    | \$ 573 |

**NOTE 22. SUBSIDIARY PREFERRED SHARES**

In connection with our acquisition of a controlling financial interest in IAHGames, we had assumed Class A preferred shares, which were owned by the noncontrolling shareholders. As of December 31, 2011 and August 15, 2012 when we deconsolidated IAHGames, these Class A preferred shares were valued at \$1.8 million and \$1.3 million, respectively, and both represented 8.9 percent of IAHGames' accumulated voting interest. The holder of the Class A preferred shares was entitled to cumulative dividends at 10 percent per annum. The preferred shares were redeemable at the holder's option at any time after the expiration of certain licensed games, and were convertible into ordinary shares at any time. Pursuant to agreements entered into in connection with our acquisition of IAHGames in July 2010, all Class A preferred shares were to be converted to ordinary shares of IAHGames at the acquisition date. The preferred shares were fully converted into ordinary shares by the closing date when we sold 60 percent of IAHGames. (See Note 6, "Divestitures", for additional information.)

As the redemption feature on the Class A preferred stock was not solely within the control of IAHGames, the amount was presented in the mezzanine section of the Consolidated Balance Sheet. Also, since the Class A preferred shares were never currently redeemable and it was not probable that they would become redeemable as a result of our acquisition of IAHGames, the subsequent adjustment for accretion was not required.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

However, the cumulative dividends and the reversal of dividends upon the conversion described above for these Class A preferred shares of \$148 thousand, \$321 thousand and \$(469) thousand for the years ended December 31, 2010, 2011 and the period from January to July 31, 2012, respectively, are included as a component of net income (loss) attributable to the noncontrolling interest in the Consolidated Statement of Operations.

**NOTE 23. EQUITY**

In accordance with Singapore law, our Company's common stock does not have a par value. In addition, we are not required to have a number of authorized common shares to be issued.

In accordance with R.O.C. law, an appropriation for legal reserve amounting to 10 percent of a company's net profit is required until the reserve equals the aggregate par value of such Taiwan company's issued capital stock. As of December 31, 2011 and 2012, the legal reserves of Hoshin GigaMedia Center Inc. ( Hoshin GigaMedia ), which represent a component of our consolidated accumulated deficit, were \$3.0 million for each period. The reserve can only be used to offset a deficit or be distributed as a stock dividend of up to 50 percent of the reserve balance when the reserve balance has reached 50 percent of the aggregate paid-in capital of Hoshin GigaMedia.

Under PRC laws and regulations, there are certain foreign exchange restrictions on our Company's PRC subsidiaries and VIE subsidiaries with respect to transferring certain of their net assets to our Company either in the form of dividends, loans or advances.

As of December 31, 2011 and 2012, our Company's total restricted net assets, which include paid up capital of PRC subsidiaries and the net assets of VIE subsidiaries in which our Company has no legal ownership, were approximately \$3.6 million and \$1.5 million, respectively.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

On May 20, 2011, our board of directors approved an \$11 million share repurchase program of GigaMedia's common stock. Under the terms of the share repurchase program, GigaMedia could repurchase up to \$11 million worth of its issued and outstanding shares during the period starting from June 1, 2011 to November 30, 2011. The repurchases could be made from time to time on the open market at prevailing market prices pursuant to a Rule 10b5-1 plan, subject to restrictions relating to volume, pricing and timing. The timing and extent of any repurchases depended upon market conditions, the trading price of GigaMedia's shares and other factors. This share repurchase program was implemented in a manner consistent with market conditions, in the interests of our shareholders, and in compliance with GigaMedia's securities trading policy and relevant Singapore and U.S. laws and regulations. During 2011, repurchases under this program amounted to approximately 5.6 million shares at a cost of \$5.8 million. All of the shares repurchased under this program were cancelled by the end of 2011.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 24. SHARE-BASED COMPENSATION**

The following table summarizes the total stock-based compensation expense recognized in our Consolidated Statements of Income (Loss):

| (in US\$ thousands)  | 2010     | 2011     | 2012   |
|--|----------|----------|--------|
| Cost of online game and service revenues   | \$ 10    | \$       | \$     |
| Product development & engineering expenses   | 18       |          |        |
| Selling and marketing expenses   | 64       | 62       | 20     |
| General and administrative expenses  | 2,922    | 1,103    | 159    |
| Pre-tax stock-based compensation expense   | 3,014    | 1,165    | 179    |
| Income tax benefit   | (90)     | (109)    | (41)   |
| Total stock-based compensation expense reported in continuing operations               | \$ 2,924 | \$ 1,056 | \$ 138 |
| Total stock-based compensation expense reported in discontinued operations, net of tax | \$       | \$       | \$     |

There were no significant capitalized stock-based compensation costs at December 31, 2011 and 2012.

***(a) Overview of Stock-Based Compensation Plans******2002 Employee Share Option Plan***

At the June 2002 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2002 Employee Share Option Plan (the 2002 Plan) under which up to three million common shares of our Company have been reserved for issuance. All employees, officers, directors, supervisors, advisors, and consultants of our Company are eligible to participate in the 2002 Plan. The 2002 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the exercise price for the option grants, the eligible individuals who are to receive option grants, the time or times when options grants are to be made, the number of shares subject to grant and the vesting schedule. The maximum contractual term for the options under the 2002 Plan is 10 years.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***2004 Employee Share Option Plan***

At the June 2004 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2004 Employee Share Option Plan (the 2004 Plan ) under which up to seven million common shares of our Company have been reserved for issuance. All employees, officers, directors, supervisors, advisors, and consultants of our Company are eligible to participate in the 2004 Plan. The 2004 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the exercise price for the option grants, the eligible individuals who are to receive option grants, the time or times when options grants are to be made, the number of shares subject to grant and the vesting schedule. The maximum contractual term for the options under the 2004 Plan is 10 years.

***2006 Equity Incentive Plan***

At the June 2006 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2006 Equity Incentive Plan (the 2006 Plan ) under which up to one million common shares of our Company have been reserved for issuance. The 2006 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2006 Plan. The maximum contractual term for the options under the 2006 Plan is 10 years.

***2007 Equity Incentive Plan***

At the June 2007 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2007 Equity Incentive Plan (the 2007 Plan ) under which up to two million common shares of our Company have been reserved for issuance. The 2007 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2007 Plan. The maximum contractual term for the options under the 2007 Plan is 10 years.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***2008 Equity Incentive Plan***

At the June 2008 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2008 Equity Incentive Plan (the 2008 Plan ) under which up to one million common shares of our Company have been reserved for issuance. The 2008 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2008 Plan. The maximum contractual term for the options under the 2008 Plan is 10 years.

***2008 Employee Share Purchase Plan***

At the June 2008 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2008 Employee Share Purchase Plan (the 2008 ESPP ) under which up to two hundred thousand common shares of our Company were reserved for issuance. Any person who is regularly employed by our Company or our designated subsidiaries shall be eligible to participate in the 2008 ESPP. Pursuant to the 2008 ESPP, our Company would offer the shares to qualified employees on favorable terms. Employees are also subject to certain restrictions on the amount that may be invested to purchase the shares and to other terms and conditions of the 2008 ESPP. The 2008 ESPP is administered by a committee designated by the board of directors. As of December 31, 2012, no shares have been subscribed by qualified employees under the 2008 ESPP.

***2009 Equity Incentive Plan***

At the June 2009 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2009 Equity Incentive Plan (the 2009 Plan ) under which up to one and a half million common shares of our Company have been reserved for issuance. The 2009 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2009 Plan. The maximum contractual term for the options under the 2009 Plan is 10 years.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

***2009 Employee Share Purchase Plan***

At the June 2009 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2009 Employee Share Purchase Plan (the 2009 ESPP ) under which up to two hundred thousand common shares of our Company have been reserved for issuance. To be eligible, employees must be regularly employed by us or our designated subsidiaries. Employees are also subject to certain restrictions on the amount that may be invested to purchase the shares and to other terms and conditions of the 2009 ESPP. The 2009 ESPP is administered by a committee designated by the board of directors. As of December 31, 2012, no shares have been issued to employees under the 2009 ESPP.

***2010 Equity Incentive Plan***

At the June 2010 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2010 Equity Incentive Plan (the 2010 Plan ) under which up to one million common shares of our Company have been reserved for issuance. The 2010 Plan is administered by a committee designated by the board of directors. The committee as plan administrator has complete discretion to determine the grant of awards under the 2010 Plan. The maximum contractual term for the options under the 2010 Plan is 10 years.

***2010 Employee Share Purchase Plan***

At the June 2010 annual general meeting of shareholders, the shareholders of our Company approved the GigaMedia Limited 2010 Employee Share Purchase Plan (the 2010 ESPP ) under which up to two hundred thousand common shares of our Company have been reserved for issuance. To be eligible, employees must be regularly employed by us or our designated subsidiaries. Employees are also subject to certain restrictions on the amount that may be invested to purchase the shares and to other terms and conditions of the 2010 ESPP. The 2010 ESPP is administered by a committee designated by the board of directors. As of December 31, 2012, no shares have been issued to employees under the 2010 ESPP.



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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Summarized below are the general terms of our stock-based compensation plans, for which awards have been granted as of December 31, 2012.

| Stock-Based compensation plan | Granted awards           | Vesting schedule                        | Options exercise price | RSUs grant date fair value |
|-------------------------------|--------------------------|---|------------------------|----------------------------|
| 2002 Plan                     | 3,000,000                | immediately upon granting               | \$0.79                 |                            |
| 2004 Plan                     | 7,703,185 <sup>(1)</sup> | immediately upon granting to four years | \$0.79~\$2.55          |                            |
| 2006 Plan                     | 1,197,333 <sup>(2)</sup> | immediately upon granting to four years | \$0.8101~\$16.6        | \$2.91~\$16.01             |
| 2007 Plan                     | 3,205,217 <sup>(3)</sup> | immediately upon granting to four years | \$1.2~\$18.17          | \$2.47~\$15.35             |
| 2008 Plan                     | 1,000,000                | immediately upon granting to six years  | \$2.47~\$4.24          |                            |
| 2009 Plan                     | 2,500,000 <sup>(4)</sup> | immediately upon granting to four years | \$0.955~\$2.47         |                            |
| 2010 Plan                     | 1,600,000 <sup>(5)</sup> | three years                             | \$0.8101~\$1.05        |                            |
| 2011 Plan                     |                          |   |                        |                            |

(1) The granted awards, net of forfeited or canceled shares, were within reserved shares of seven million common shares.

(2) The granted awards, net of forfeited or canceled shares, were within reserved shares of one million common shares.

(3) The granted awards, net of forfeited or canceled shares, were within reserved shares of two million common shares.

(4) The granted awards, net of forfeited or canceled shares, were within reserved shares of one and a half million common shares.

(5) The granted awards, net of forfeited or canceled shares, were within reserved shares of one million common shares.

Options and Restricted Stock Units ( RSUs ) generally vest over the schedule described above. Certain RSUs provide for accelerated vesting if there is a change in control. All options and RSUs are expected to be settled by issuing new shares.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**(b) Options**

In 2010, 2011 and 2012, 200,500, 0 and 0 options were exercised, and cash received from the exercise of stock options was \$0.2 million, \$0 and \$0, respectively, which resulted in no significant tax benefit realized on a consolidated basis.

Our Company uses the Black-Scholes option-pricing model to estimate the fair value of stock options granted to employees. The following table summarizes the assumptions used in the model for options granted during 2011 and 2012:

|   | 2011          | 2012          |
|---|---------------|---------------|
| Option term (years)                           | 5.99          | 5.73          |
| Volatility                                    | 58.89%~63.03% | 59.76%~67.02% |
| Weighted-average volatility                   | 59%           | 62%           |
| Risk-free interest rate                       | 2.14%~2.31%   | 0.885%~1.152% |
| Dividend yield                                | 0%            | 0%            |
| Weighted-average fair value of option granted | \$0.60        | \$0.54        |

Option term. The expected term of the options granted represents the period of time that they are expected to be outstanding. Our Company estimates the expected term of options granted based on historical experience with grants and option exercises.

Expected volatility rate. An analysis of historical volatility was used to develop the estimate of expected volatility.

Risk-free interest rate. The risk-free interest rate is based on yields of U.S. Treasury bonds for the expected term of the options.

Expected dividend yield. The dividend yield is based on our Company's current dividend yield.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Option transactions during the last three years are summarized as follows:

|  | 2010                         |                              | 2011                         |                              | 2012                         |                              | Weighted-Average Remaining Contractual Term | Aggregate Intrinsic Value (in thousands) |
|--|------------------------------|------------------------------|------------------------------|------------------------------|------------------------------|------------------------------|---|--|
|  | Weighted Avg. Exercise Price | No. of Shares (in thousands) | Weighted Avg. Exercise Price | No. of Shares (in thousands) | Weighted Avg. Exercise Price | No. of Shares (in thousands) |   |  |
| Balance at January 31                      | \$ 2.36                      | 7,689                        | \$ 2.33                      | 9,780                        | \$ 2.13                      | 9,493                        |   |  |
| Options granted                            | 2.47                         | 2,565                        | 1.06                         | 1,060                        | 0.96                         | 2,070                        |   |  |
| Options exercised                          | 0.87                         | (201)                        |                              |                              |                              |                              |   |  |
| Options Forfeited / canceled / expired     | 5.66                         | (273)                        | 2.72                         | (1,347)                      | 1.74                         | (2,353)                      |   |  |
| Balance at December 31                     | \$ 2.33                      | 9,780                        | \$ 2.13                      | 9,493                        | \$ 1.97                      | 9,210                        | \$ 3.90                                     | 890                                      |
| Exercisable at December 31                 | \$ 2.04                      | 7,190                        | \$ 2.19                      | 7,754                        | \$ 2.15                      | 7,584                        | \$ 2.69                                     | 882                                      |
| Vested and expected to vest at December 31 | \$ 2.33                      | 9,780                        | \$ 2.13                      | 9,493                        | \$ 1.97                      | 9,210                        | \$ 3.90                                     | 890                                      |

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between GigaMedia's closing stock price on the last trading day of 2012 and the fair value of the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had they exercised their options on December 31, 2012. This amount changes based on the fair market value of GigaMedia's stock. The total intrinsic value of options exercised for the years ended December 31, 2010, 2011, and 2012 were \$0.3 million, \$0, and \$0, respectively.

As of December 31 2012, there was approximately \$707 thousand of unrecognized compensation cost related to nonvested options. That cost is expected to be recognized over a period of 2.7 years.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The following table sets forth information about stock options outstanding at December 31, 2012:

| Exercise price | Options outstanding             |                                 | Weighted<br>average<br>contractual life | Option currently exercisable    |                                 |
|----------------|---------------------------------|---------------------------------|---|---------------------------------|---------------------------------|
|                | No. of Shares<br>(in thousands) | No. of Shares<br>(in thousands) |   | No. of Shares<br>(in thousands) | No. of Shares<br>(in thousands) |
| Under \$1      | 6,211                           |                                 | 2.87 years                              | Under \$1                       | 5,191                           |
| \$1~\$10       | 2,383                           |                                 | 6.40 years                              | \$1~\$10                        | 1,777                           |
| \$10~\$20      | 616                             |                                 | 4.65 years                              | \$10~\$20                       | 616                             |
|                | 9,210                           |                                 |   |                                 | 7,584                           |

*(c) RSUs*

Nonvested RSUs during 2011 and 2012 were as follows:

|                          | 2011                                    |   | 2012                                    |   |
|--------------------------|---|---|---|---|
|                          | Number<br>of<br>units<br>(in thousands) | Weighted-<br>average<br>grant date<br>fair<br>value | Number<br>of<br>units<br>(in thousands) | Weighted-<br>average<br>grant date<br>fair<br>value |
| Nonvested at January 1   | 390                                     | \$ 10.99  |   | \$  |
| Granted                  | 323                                     | 3.01  |   |   |
| Vested                   | (80)                                    | 2.99  |   |   |
| Forfeited                | (633)                                   | 7.92  |   |   |
| Nonvested at December 31 |   |   |   |   |

The fair value of RSUs is determined and fixed on the grant date based on our stock price. The fair value of RSUs granted during the years ended December 31, 2010, 2011 and 2012 was \$0.3 million, \$1.0 million and \$0, respectively. The total fair value of RSUs vested during the years ended December 31, 2010, 2011 and 2012 was \$1.0 million, \$0.2 million and \$0, respectively, which resulted in no significant tax benefit realized on a consolidated basis.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

As of December 31 2012, there was no unrecognized compensation cost related to nonvested RSUs. Our Company received no cash from employees as a result of employee stock award vesting and the forfeiture of RSUs during 2010, 2011 and 2012.

**NOTE 25. INCOME TAXES**

Income (loss) from continuing operations before income taxes by geographic location is as follows:

| (in US\$ thousands) | 2010     | 2011        | 2012        |
|---------------------|----------|-------------|-------------|
| U.S. operations     | \$ 5,678 | \$ (1,444)  | \$ (418)    |
| Non-U.S. operations | 2,990    | (66,191)    | (12,507)    |
|                     | \$ 8,668 | \$ (67,635) | \$ (12,925) |

Income tax provision (benefit) from continuing operations by geographic location is as follows:

| (in US\$ thousands) | 2010     | 2011     | 2012   |
|---------------------|----------|----------|--------|
| U.S. operations     | \$ 4,992 | \$ (616) | \$ 23  |
| Non-U.S. operations | 2,268    | 371      | 648    |
|                     | \$ 7,260 | \$ (245) | \$ 671 |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The components of income tax provision (benefit) from continuing operations by taxing jurisdiction are as follows:

| (in US\$ thousands)                         | 2010            | 2011            | 2012          |
|---|-----------------|-----------------|---------------|
| <b>U.S. Federal :</b>                       |                 |                 |               |
| Current                                     | \$ 4,244        | \$ (493)        | \$            |
| Deferred                                    | 20              |                 |               |
|   | \$ 4,264        | \$ (493)        | \$            |
| <b>U.S. State and Local :</b>               |                 |                 |               |
| Current                                     | \$ 617          | \$ (123)        | \$ 23         |
| Deferred                                    | 111             |                 |               |
|   | \$ 728          | \$ (123)        | \$ 23         |
| <b>Non - U.S. :</b>                         |                 |                 |               |
| Current                                     | \$ 2,032        | \$ 77           | \$ 602        |
| Deferred                                    | 236             | 294             | 46            |
|   | \$ 2,268        | \$ 371          | \$ 648        |
| <b>Total income tax provision (benefit)</b> | <b>\$ 7,260</b> | <b>\$ (245)</b> | <b>\$ 671</b> |

A reconciliation of our effective tax rate related to continuing operations to the statutory U.S. federal tax rate is as follows:

|   | 2010     | 2011     | 2012     |
|---|----------|----------|----------|
| Federal statutory rate  | 34.00%   | 34.00%   | 34.00%   |
| State and local - net of federal tax benefit                                | 6.69%    | 5.45%    | 5.45%    |
| Foreign tax differential  | (88.75%) | (14.58%) | (15.77%) |
| Permanent differences   | 31.58%   | (2.75%)  | (19.30%) |
| Change in valuation allowance   | 52.73%   | (21.70%) | (4.00%)  |
| Tax effect of earnings for equity method investees and certain subsidiaries | 42.72%   | (0.02%)  | (4.38%)  |
| Other   | 4.79%    | (0.06%)  | (1.19%)  |
| Effective rate  | 83.76%   | 0.34%    | (5.19%)  |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In 2010, the primary reason for the increase in the income tax provision and the effective income tax rate was due to the sale of 60 percent of our gaming software and service business. (See Note 6, "Divestiture", for additional information.) The income tax provision related to the sale of the gaming software and service business in 2010 was approximately \$6.1 million, which represented approximately 70 percent of our income from continuing operations.

The provision (benefit) for income taxes attributable to discontinued operations was \$0 for each of the years ended December 31, 2010, 2011 and 2012, respectively.

Significant components of our deferred tax assets consist of the following:

| (in US\$ thousands)              | December 31 |          |
|----------------------------------|-------------|----------|
|                                  | 2011        | 2012     |
| Net operating loss carryforwards | \$ 9,901    | \$ 3,248 |
| Loss on equity method investment | 15,621      | 15,621   |
| Share-based compensation         | 190         | 234      |
| Impairment charges               | 97          | 177      |
| Pension expense                  | 29          | 26       |
| Depreciation                     | 111         | 37       |
| Other                            | 66          | (61)     |
|                                  | 26,015      | 19,282   |
| Less: valuation allowance        | (25,256)    | (18,333) |
| Deferred tax assets - net        | \$ 759      | \$ 949   |

As of December 31, 2011 and 2012, \$759 thousand and \$840 thousand, respectively, of the net deferred tax assets were reported as current and included in other current assets on the balance sheet.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Significant components of our deferred tax liabilities consist of the following:

| (in US\$ thousands)   | December 31     |               |
|---|-----------------|---------------|
|   | 2011            | 2012          |
| Depreciation and amortization                                   | \$ 344          | \$ 255        |
| Tax effect on undistributed earnings of equity method investees | 662             | 306           |
| <b>Deferred tax liabilities</b>                                 | <b>\$ 1,006</b> | <b>\$ 561</b> |

As of December 31, 2011 and 2012, \$1.0 million and \$561 thousand, respectively, of deferred tax liabilities were reported as non-current deferred tax liabilities and included in other liabilities.

A reconciliation of the beginning and ending amounts of our valuation allowance on deferred tax assets for the years ended December 31, 2010, 2011 and 2012 are as follows:

| (in US\$ thousands)                                    | 2010            | 2011             | 2012             |
|--|-----------------|------------------|------------------|
| Balance at beginning of year                           | \$ 1,068        | \$ 7,402         | \$ 25,256        |
| Subsequent reversal/utilization of valuation allowance | (12)            | (270)            | (4)              |
| Additions to valuation allowance                       | 4,583           | 15,597           | 214              |
| Divestitures   | (874)           |                  | (7,026)          |
| Acquisitions   | 2,624           | 2,491            |                  |
| Exchange differences                                   | 13              | 36               | (107)            |
| <b>Balance at end of year</b>                          | <b>\$ 7,402</b> | <b>\$ 25,256</b> | <b>\$ 18,333</b> |

In 2010, the valuation allowance on the deferred tax assets increased by \$6.3 million to \$7.4 million primarily due to the acquisition of IAHGAMES. IAHGAMES had successive losses in prior years and therefore we do not believe that sufficient objective, positive evidence existed at the date of our acquisition to conclude that the realization of the deferred tax assets that we acquired from IAHGAMES was more likely than not. We also provided a valuation allowance against deferred tax assets related to certain of our other subsidiaries, as they are not likely to be able to utilize all of their deferred tax assets based on their estimated future taxable income.



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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In 2011, the valuation allowance on the deferred tax assets increased by \$17.9 million to \$25.3 million primarily due to the evaluation of the loss related to our investment in Mangas Everest. We provided a valuation allowance against the deferred tax asset related to our investment loss in Mangas Everest as we believe that the subsequent disposal of this investment will not likely offset the related deferred tax asset based on our estimation of any future disposal gain, as Mangas Everest has had successive losses, and therefore we do not believe that sufficient objective, positive evidence exists to conclude that the realization of the deferred tax asset related to our investment losses in Mangas Everest is more likely than not.

As of December 31, 2012, we had net operating loss carryforwards available to offset future income, amounting to \$13.5 million. Below is the breakdown of the expiration of the net operating loss carryforwards in major jurisdictions:

| Jurisdiction | Amount | Expiring year |
|--------------|--------|---------------|
| Hong Kong    | 9,174  | indefinite    |
| Taiwan       | 4,333  | 2021          |
|              | 13,507 |               |

Under Singapore tax regulations, foreign-sourced dividend income used for capital expenditures, including investments, and repayment of borrowings, would not be deemed as remitted to Singapore and is therefore not taxable.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Uncertain Tax Positions**

A reconciliation of the beginning and ending amount of unrecognized tax benefits (excluding the effects of accrued interest) for the years 2010, 2011 and 2012 are as follows:

| (in US\$ thousands)                     | 2010     | 2011     | 2012     |
|---|----------|----------|----------|
| Balance at beginning of year            | \$ 702   | \$ 1,667 | \$ 2,079 |
| Acquisition of IAHGames                 | 535      |          |          |
| Increase for prior year tax positions   | 194      | 451      | 116      |
| Increase for current year tax positions | 323      |          |          |
| Decrease due to settlement              | (166)    |          |          |
| Deconsolidation of IAHGames             |          |          | (1,072)  |
| Exchange differences                    | 79       | (39)     | 45       |
| Balance at end of year                  | \$ 1,667 | \$ 2,079 | \$ 1,168 |

As of December 31, 2010, 2011 and 2012, there were approximately \$1.7 million, \$2.1 million and \$1.2 million of unrecognized tax benefits that if recognized would affect the effective tax rate.

Interest and penalties related to income tax liabilities are included in income tax expense. In 2010, 2011 and 2012, there were no significant interest and penalties recognized in income tax expense.

Our major tax jurisdictions are located in Taiwan, the PRC, and Singapore. As of December 31, 2012, the income tax filings under tax jurisdictions located in Taiwan have been examined for the years through 2008 and for 2010, but we have filed appeals for the 2006, 2007 and 2008 tax filings. Our Company also files income tax returns in the United States federal and state jurisdictions. The tax authority in the U.S. is currently examining the 2012 tax filing.

In 2010, 2011 and 2012, our unrecognized tax benefits were related to research and development credits and were also related to amortization of goodwill and intangible assets resulting from the acquisition of FunTown. For research and development credits, these unrecognized tax benefits were settled with tax authorities through the 2008 tax filings. For amortization of goodwill and intangible assets resulting from the acquisition of FunTown, the income tax authority has made decisions on the amortization for our 2006, 2007 and 2008 tax filings. We have filed appeals against the unfavorable parts of the decision regarding these amortization adjustments, appending further response from the tax authority.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In 2010 and 2011, our unrecognized tax benefits increased due to the acquisition of IAHGames. These unrecognized tax benefits primarily related to certain related party transactions.

The amount of unrecognized tax benefits may increase or decrease in the future for various reasons such as current year tax positions, expiration of statutes of limitations, litigation, legislative activity, or other changes in facts regarding realizability. However, at this time, an estimate of the potential range of change cannot be reasonably made.

**NOTE 26. RELATED-PARTY TRANSACTIONS**

In 2010 and 2011, to support our current operations we had short-term indebtedness from Waterland Financial Holdings ( Waterland ), a key manager of which was one of our directors. The largest amounts of outstanding short-term indebtedness to Waterland during the years ended December 31, 2010 and 2011 were \$1.5 million and \$1.7 million, respectively. As of December 31, 2011 and 2012, we did not have any indebtedness owed to Waterland.

We, through IAHGames, made an equity investment in Monsoon in connection with our acquisition of IAHGames with effect from July 1, 2010. In 2010, prior to our acquisition, IAHGames loaned \$5.0 million to Monsoon to support Monsoon's current operations at interest of 7 percent per annum. In addition, from September to December 2010, we loaned an additional \$5.1 million to Monsoon to support its operation at an interest rate of 7 percent per annum. The largest amount outstanding to Monsoon from July 1, 2010 through August 31, 2011, after which we began to consolidate Monsoon, was \$10.3 million. As of August 31, 2011, the balance of this loan receivable was \$3.2 million, after being reduced in connection with absorbing additional losses of Monsoon as discussed in more detail in Note 16, Investments .

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

During 2011, our Company entered into loan agreements in the aggregate of \$5.2 million with Mangas Everest, with interest rates of 3 percent per annum. As of December 31, 2011, the balance of this loan receivable was nil after being reduced in connection with absorbing additional losses of Mangas Everest (as discussed in more detail in Note 16, Investments ) and considering the financial status of Mangas Everest, from which we do not expect to collect all principal and interest. We also reversed the interest recognized previously on these loans and ceased to recognize interest income going forward.

**NOTE 27. COMMITMENTS AND CONTINGENCIES****Commitments*****(a) Operating Leases***

We rent certain properties which are used as office premises under lease agreements that expire at various dates through 2016. The following table sets forth our future aggregate minimum lease payments required under these operating leases, as of December 31, 2012:

| (in US\$ thousands) | Amount   |
|---------------------|----------|
| 2013                | \$ 930   |
| 2014                | 798      |
| 2015                | 681      |
| 2016                | 114      |
|                     | \$ 2,523 |

Rental expense for operating leases amounted to \$3.0 million, \$2.5 million and \$1.8 million for the years ended December 31, 2010, 2011 and 2012, respectively.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**(b) License Agreements**

We have contractual obligations under various license agreements to pay the licensors license fees and minimum guarantees against future royalties. The following table summarizes the committed license fees and minimum guarantees against future royalties set forth in our significant license agreements as of December 31, 2012.

| (in US\$ thousands)               | License fees | Minimum<br>guarantees<br>against future<br>royalties | Total    |
|-----------------------------------|--------------|--|----------|
| <b>Minimum required payments:</b> |              |  |          |
| In 2013                           | \$ 189       | \$ 100   | \$ 289   |
| After 2013                        | 5,700        | 1,500  | 7,200    |
|                                   | \$ 5,889     | \$ 1,600   | \$ 7,489 |

The initial minimum guarantees against future royalties and license fees are not required to be paid until the licensed games are commercially released or until certain milestones are achieved, as stipulated in the individual license agreements. The remaining minimum guarantees are generally required to be paid within three years subsequent to the commercial release dates of the licensed games.

**(c) Guaranty**

In 2008, Cambridge Interactive Development Corp. ( CIDC ), a then wholly owned subsidiary of GigaMedia, entered into a lease agreement (the CIDC Lease ) for an office in Delaware. The term of the CIDC Lease is for the period from October 1, 2008 through September 30, 2014. Pursuant to the CIDC Lease, CIDC deposited \$689,789 with a bank in exchange for a letter of credit issued by the bank (the CIDC L/C ) and GigaMedia's guaranty of all of CIDC's obligations under the CIDC Lease.

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

In July 2012, we entered into an agreement with BEG to sell and assign our remaining ownership interest in Mangas Everest (including the CIDC lease) (the Mangas Agreement). Pursuant to the Mangas Agreement, BEG was to use all its reasonable efforts to procure the cancellation and return of the CIDC L/C to GigaMedia and the landlord's release of GigaMedia's lease guaranty by September 30, 2012; and unless and until BEG procures the cancellation and return of the CIDC L/C and landlord's release of GigaMedia's lease guaranty, BEG is obligated to indemnify and hold GigaMedia (and any Affiliate thereof) harmless from any and all losses, costs and expenses that may be borne by GigaMedia (and any Affiliate thereof) arising under or in connection with the CIDC L/C and/or GigaMedia's lease guaranty.

In accordance with the Mangas Agreement, BEG procured that the bank cancel the CIDC L/C and issue to BEG a new letter of credit under the same terms and conditions as the CIDC L/C. BEG, however, did not obtain the landlord's consent to release us from our lease guaranty within the allotted time. BEG's major shareholders, therefore, issued a separate guaranty to us wherein they are obligated to indemnify and hold GigaMedia (and any Affiliate thereof) harmless from any and all losses, costs and expenses arising under or in connection with the CIDC Lease. GigaMedia's commitment amount under this lease guaranty will be reduced as Mangas Everest's subsidiary who assumed the CIDC Lease makes its monthly rental payments. The leasee is current on its monthly payments through March 2013.

**Contingencies**

We are subject to legal proceedings and claims that arise in the normal course of business. We believe the ultimate liabilities with respect to these actions will not have a material adverse effect on our financial condition, results of operations or cash flows

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Note 28. SEGMENT INFORMATION**

*Segment data*

We have identified two reportable segments: an online gaming software and service business segment (through July 31, 2012) and an Asian online game and service business segment. The online gaming software and service business segment mainly derives its revenues from developing and licensing online games of chance and skill. Subsequent to the sale transaction with BEG through our disposal of this investment in July 2012, we accounted for our 40 percent percentage ownership interest in our gaming software and service business under the equity method accounting, and record gains or losses from our equity method investment in one line on our Consolidated Statement of Operations. The Asian online game and service business segment mainly derives its revenues from recognizing the usage of game playing time or in-game items by the end-users. Our new cloud computing service business described in Note 1 has not met any of the quantitative thresholds required to be reportable.

Our management relies on an internal management reporting process that provides revenue and segment information for making financial decisions and allocating resources. The results are based on our method of internal reporting and are not necessarily in conformity with GAAP. Management measures the performance of each segment based on several metrics, including revenues and income or loss from operations.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

Financial information for each reportable segment was as follows as of and for the years ended December 31, 2010, 2011, and 2012:

| (in US\$ thousands)   | Gaming<br>software and<br>service | Asian online<br>game and<br>service | Total       |
|---|-----------------------------------|-------------------------------------|-------------|
| <b>2010:</b>  |                                   |                                     |             |
| <b>Segment profit or loss:</b>                                  |                                   |                                     |             |
| Net revenue from external customers                             | \$ 25,820                         | \$ 38,862                           | \$ 64,682   |
| Income (loss) from operations                                   | \$ 78                             | \$ (31,554)                         | \$ (31,476) |
| Share-based compensation  | \$ 80                             | \$ 342                              | \$ 422      |
| Impairment loss on prepaid licensing fees and intangible assets | \$                                | \$ 2,200                            | \$ 2,200    |
| Impairment loss on property, plant and equipment                | \$                                | \$ 278                              | \$ 278      |
| Impairment loss on goodwill                                     | \$                                | \$ 2,255                            | \$ 2,255    |
| Impairment loss on deconsolidation of T2CN                      | \$                                | \$ 22,234                           | \$ 22,234   |
| Interest income   | \$ 83                             | \$ 438                              | \$ 521      |
| Interest expense  | \$ 1                              | \$ 59                               | \$ 60       |
| Foreign exchange gain (loss)                                    | \$ (29)                           | \$ 91                               | \$ 62       |
| Loss on equity method investments - net                         | \$ 9,768                          | \$ 11,002                           | \$ 20,770   |
| Impairment loss on marketable securities and investments        | \$                                | \$ 4,677                            | \$ 4,677    |
| Depreciation  | \$                                | \$ 1,556                            | \$ 1,556    |
| Amortization, including intangible assets                       | \$                                | \$ 2,696                            | \$ 2,696    |
| Income tax expense  | \$ 6,445                          | \$ 1,118                            | \$ 7,563    |
| <b>Segment assets:</b>  |                                   |                                     |             |
| Equity method investments                                       | \$ 44,472                         | \$ 20,923                           | \$ 65,395   |
| Additions to property, plant and equipment                      | \$ 1,209                          | \$ 1,534                            | \$ 2,743    |
| Additions to intangible assets                                  | \$ 1,198                          | \$ 1,114                            | \$ 2,312    |



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|                       |            |           |            |
|-----------------------|------------|-----------|------------|
| Additions to goodwill | \$         | \$ 12,188 | \$ 12,188  |
| Total assets          | \$ 168,671 | \$ 76,679 | \$ 245,350 |

The reconciliation of the segment information to GigaMedia's consolidated information was not included in the above table, as it is provided below in detail.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

| (in US\$ thousands)                                      | Gaming<br>software and<br>service | Asian online<br>game and<br>service | Total       |
|--|-----------------------------------|-------------------------------------|-------------|
| <b>2011:</b>   |                                   |                                     |             |
| <b>Segment profit or loss:</b>                           |                                   |                                     |             |
| Net revenue from external customers                      | \$                                | \$ 34,367                           | \$ 34,367   |
| Loss from operations                                     | \$ (204)                          | \$ (10,931)                         | \$ (11,135) |
| Share-based compensation                                 | \$                                | \$ 308                              | \$ 308      |
| Impairment loss on intangible assets                     | \$                                | \$ 2,583                            | \$ 2,583    |
| Impairment loss on prepaid licensing and royalty fees    | \$                                | \$ 247                              | \$ 247      |
| Impairment loss on goodwill                              | \$                                | \$ 5,097                            | \$ 5,097    |
| Interest income  | \$                                | \$ 492                              | \$ 492      |
| Interest expense   | \$ 55                             | \$ (50)                             | \$ 5        |
| Foreign exchange gain (loss)                             | \$ 6                              | \$ (282)                            | \$ (276)    |
| Loss (gain) on equity method investments - net           | \$ 49,715                         | \$ (1,846)                          | \$ 47,869   |
| Impairment loss on marketable securities and investments | \$                                | \$ 13,327                           | \$ 13,327   |
| Depreciation   | \$                                | \$ 1,790                            | \$ 1,790    |
| Amortization, including intangible assets                | \$                                | \$ 2,251                            | \$ 2,251    |
| Income tax (benefit) expense                             | \$ (934)                          | \$ 859                              | \$ (75)     |
| <b>Segment assets:</b>                                   |                                   |                                     |             |
| Equity method investments                                | \$                                | \$ 7,615                            | \$ 7,615    |
| Additions to property, plant and equipment               | \$                                | \$ 487                              | \$ 487      |
| Additions to intangible assets                           | \$                                | \$ 1,271                            | \$ 1,271    |
| Additions to goodwill                                    | \$                                | \$ 1,049                            | \$ 1,049    |
| Total assets   | \$ 4,757                          | \$ 126,038                          | \$ 130,795  |

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The reconciliation of the segment information to GigaMedia's consolidated information was not included in the above table, as it is provided below in detail.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

| (in US\$ thousands)                                      | Gaming<br>software and<br>service | Asian online<br>game and<br>service | Total       |
|--|-----------------------------------|-------------------------------------|-------------|
| <b>2012:</b>   |                                   |                                     |             |
| <b>Segment profit or loss:</b>                           |                                   |                                     |             |
| Net revenue from external customers                      | \$                                | \$ 27,470                           | \$ 27,470   |
| Income (loss) from operations                            | \$ 7                              | \$ (12,271)                         | \$ (12,264) |
| Share-based compensation                                 | \$                                | \$ 199                              | \$ 199      |
| Impairment loss on intangible assets                     | \$                                | \$ 15                               | \$ 15       |
| Impairment loss on prepaid licensing and royalty fees    | \$                                | \$ 702                              | \$ 702      |
| Impairment loss on goodwill                              | \$                                | \$ 12,489                           | \$ 12,489   |
| Contract termination costs                               | \$                                | \$ 49                               | \$ 49       |
| Interest income  | \$ 1                              | \$ 9                                | \$ 10       |
| Interest expense   | \$ 10                             | \$ 44                               | \$ 54       |
| Foreign exchange gain (loss)                             | \$ (82)                           | \$ 55                               | \$ (27)     |
| Gain on equity method investments - net                  | \$                                | \$ 234                              | \$ 234      |
| Impairment loss on marketable securities and investments | \$                                | \$ 1,193                            | \$ 1,193    |
| Depreciation   | \$                                | \$ 1,059                            | \$ 1,059    |
| Amortization, including intangible assets                | \$                                | \$ 2,181                            | \$ 2,181    |
| Income tax expense                                       | \$ 37                             | \$ 710                              | \$ 747      |
| <b>Segment assets:</b>                                   |                                   |                                     |             |
| Equity method investments                                | \$                                | \$ 5,223                            | \$ 5,223    |
| Additions to property, plant and equipment               | \$                                | \$ 318                              | \$ 318      |
| Additions to intangible assets                           | \$                                | \$ 1,679                            | \$ 1,679    |
| Total assets   | \$ 3,685                          | \$ 78,613                           | \$ 82,298   |

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The reconciliation of the segment information to GigaMedia's consolidated information was not included in the above table, as it is provided below in detail.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

The reconciliations of segment information to GigaMedia's consolidated totals are as follows:

| (in US\$ thousands)   | 2010        | 2011        | 2012        |
|---|-------------|-------------|-------------|
| <b>Income (loss) from operations:</b>                         |             |             |             |
| Total segments  | \$ (31,476) | \$ (11,135) | \$ (12,264) |
| Adjustment*   | (16,220)    | (8,794)     | (8,310)     |
| Total GigaMedia consolidated                                  | \$ (47,696) | \$ (19,929) | \$ (20,574) |
| <b>Share-based compensation</b>                               |             |             |             |
| Total segments  | \$ 422      | \$ 308      | \$ 199      |
| Adjustment*   | 2,592       | 857         | (20)        |
| Total GigaMedia consolidated                                  | \$ 3,014    | \$ 1,165    | \$ 179      |
| <b>Impairment loss on intangible assets:</b>                  |             |             |             |
| Total segments  | \$ 1,330    | \$ 2,583    | \$ 15       |
| Adjustment*   |             |             |             |
| Total GigaMedia consolidated                                  | \$ 1,330    | \$ 2,583    | \$ 15       |
| <b>Impairment loss on prepaid licensing and royalty fees:</b> |             |             |             |
| Total segments  | \$ 870      | \$ 247      | \$ 702      |
| Adjustment*   |             |             |             |
| Total GigaMedia consolidated                                  | \$ 870      | \$ 247      | \$ 702      |
| <b>Impairment loss on property, plant and equipment:</b>      |             |             |             |
| Total segments  | \$ 278      | \$          | \$          |
| Adjustment*   |             |             |             |
| Total GigaMedia consolidated                                  | \$ 278      | \$          | \$          |
| <b>Interest income:</b>                                       |             |             |             |
| Total segments  | \$ 521      | \$ 492      | \$ 10       |
| Adjustment*   | 435         | 270         | 273         |
| Total GigaMedia consolidated                                  | \$ 956      | \$ 762      | \$ 283      |
| <b>Interest expense:</b>                                      |             |             |             |
| Total segments  | \$ 60       | \$ 5        | \$ 54       |
| Adjustment*   | 310         | 421         | 193         |
| Total GigaMedia consolidated                                  | \$ 370      | \$ 426      | \$ 247      |

|  |    |          |                  |
|--|----|----------|------------------|
| <b>Gain on sales of marketable securities:</b> |    |          |                  |
| Total segments                                 | \$ | \$ 6,299 | \$ 5,665         |
| Adjustments*                                   |    |          |                  |
| Total GigaMedia consolidated                   | \$ | \$ 6,299 | \$ 5,665         |
| <b>Foreign exchange gain (loss):</b>           |    |          |                  |
| Total segments                                 | \$ | 62       | \$ (276) \$ (27) |
| Adjustments*                                   |    | (668)    | (89) 461         |
| Total GigaMedia consolidated                   | \$ | (606)    | \$ (365) \$ 434  |

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

| (in US\$ thousands)  | 2010       | 2011       | 2012       |
|--|------------|------------|------------|
| <b>Impairment loss on marketable securities and investments:</b> |            |            |            |
| Total segments   | \$ 4,677   | \$ 13,327  | \$ 1,193   |
| Adjustment*  |            |            |            |
| Total GigaMedia consolidated                                     | \$ 4,677   | \$ 13,327  | \$ 1,193   |
| <b>Depreciation:</b>   |            |            |            |
| Total segments   | \$ 1,556   | \$ 1,790   | \$ 1,059   |
| Adjustments*   | 536        | 290        | 165        |
| Total GigaMedia consolidated                                     | \$ 2,092   | \$ 2,080   | \$ 1,224   |
| <b>Amortization:</b>   |            |            |            |
| Total segments   | \$ 2,696   | \$ 2,251   | \$ 2,181   |
| Adjustments*   | 83         | 63         | 23         |
| Total GigaMedia consolidated                                     | \$ 2,779   | \$ 2,314   | \$ 2,204   |
| <b>Income tax expense (benefit):</b>                             |            |            |            |
| Total segments   | \$ 7,563   | \$ (75)    | \$ 747     |
| Adjustments*   | (303)      | (170)      | (76)       |
| Total GigaMedia consolidated                                     | \$ 7,260   | \$ (245)   | \$ 671     |
| <b>Additions to property, plant and equipment:</b>               |            |            |            |
| Total segments   | \$ 2,743   | \$ 487     | \$ 318     |
| Adjustments**  | 1,041      | 281        | 111        |
| Total GigaMedia consolidated                                     | \$ 3,784   | \$ 768     | \$ 429     |
| <b>Additions to intangible assets:</b>                           |            |            |            |
| Total segments   | \$ 2,312   | \$ 1,271   | \$ 1,679   |
| Adjustments**  | 5          | 3          |            |
| Total GigaMedia consolidated                                     | \$ 2,317   | \$ 1,274   | \$ 1,679   |
| <b>Total assets:</b>   |            |            |            |
| Total segments   | \$ 245,350 | \$ 130,795 | \$ 82,298  |
| Adjustment**   | 22,239     | 60,911     | 58,096     |
| Total GigaMedia consolidated                                     | \$ 267,589 | \$ 191,706 | \$ 140,394 |

\* Adjustment items include corporate and certain back-office costs and expenses not attributable to any specific segment.



\*\* Adjustment items include total corporate assets, discontinued operations and eliminations.

***Major Customers***

No single customer represented 10 percent or more of GigaMedia's total net revenues in any period presented.

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## GIGAMEDIA LIMITED

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**Geographic Information**

Revenues by geographic area are attributed by country of the server location. Revenue from unaffiliated customers by geographic region is as follows:

| (in US\$ thousands)         |           |           |           |
|-----------------------------|-----------|-----------|-----------|
| Geographic region / country | 2010      | 2011      | 2012      |
| Canada                      | \$ 25,820 | \$        | \$        |
| Taiwan                      | 19,449    | 21,214    | 18,744    |
| PRC                         | 9,885     |           |           |
| Hong Kong                   | 4,026     | 5,061     | 4,703     |
| Singapore                   | 3,702     | 4,150     | 2,004     |
| Malaysia                    | 1,603     | 2,228     | 1,550     |
| Thailand                    |           | 1,447     | 204       |
| Others                      | 197       | 267       | 265       |
|                             | \$ 64,682 | \$ 34,367 | \$ 27,470 |

Net long-lived assets by geographic region are as follows:

| (in US\$ thousands)         |          | December 31, |          |
|-----------------------------|----------|--------------|----------|
| Geographic region / country | 2010     | 2011         | 2012     |
| Taiwan                      | \$ 3,130 | \$ 2,375     | \$ 1,932 |
| PRC                         | 921      | 763          |          |
| Hong Kong                   | 213      | 107          | 17       |
| Singapore                   | 902      | 551          |          |
| Malaysia                    | 20       |              |          |
| Thailand                    |          | 380          |          |
| Other                       | 115      | 112          |          |
|                             | \$ 5,301 | \$ 4,288     | \$ 1,949 |

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GIGAMEDIA LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

YEARS ENDED DECEMBER 31, 2010, 2011 AND 2012

**NOTE 29. SUBSEQUENT EVENT**

On April 17, 2013, we entered into a settlement agreement (the Settlement Agreement) with IAHGames, IAHGames management, and MCIL. Pursuant to the terms of the Settlement Agreement, either IAHGames or IAHGames management is to pay us \$2,258 thousand, which includes interest, to fulfill IAHGames obligation under the Spring Asia Share Purchase Agreement executed in July 2012. In addition, pursuant to the terms of the Settlement Agreement, MCIL is to purchase all of our remaining shares in IAHGames for \$1,000 thousand, pursuant to MCIL's April 15, 2013 exercise of a call option which was included within the IAH Share Purchase Agreement executed in July 2012. The payment date for the transactions outlined in the Settlement Agreement was agreed by the parties to occur in early May 2013.

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