

SUBAYE, INC.  
Form 10-Q  
February 16, 2010

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

FORM 10-Q

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

For the quarterly period ended December 31, 2009

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number: 333-62236

SUBAYE, INC.

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction  
of incorporation or organization)

35-2089848  
(I.R.S. Employer  
Identification No.)

349 Dabeilu, Shiqiao, Panyu,  
Guangzhou,  
Guangdong, China 511400  
(Address of principal executive offices) (Zip Code)

86 2039990266  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered under Section 12(g) of the Act:

Common stock, par value \$.001 per share  
(Title of class)

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  
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

Edgar Filing: SUBAYE, INC. - Form 10-Q

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer (Do not check if a smaller reporting company)	<input type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>

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

As of February 12, 2010, the registrant had 6,664,131 shares of its common stock issued and outstanding.

---

## TABLE OF CONTENTS

	PAGE
<b>PART I</b>	
ITEM 1. Condensed Consolidated Financial Statements	F-1
Condensed Consolidated Balance Sheets as of December 31, 2009 (Unaudited) and September 30, 2009	F-1
Unaudited Condensed Consolidated Statements of Operations for the Three Months Ended December 31, 2009 and December 31, 2008	F-2
Unaudited Condensed Consolidated Statements of Cash Flows for the Three Months Ended December 31, 2009 and December 31, 2008	F-3
Notes to the Condensed Consolidated Financial Statements	F-4
ITEM 2. Management's Discussion and Analysis of Financial Condition and Plan of Operation	F-17
ITEM 3. Quantitative and Qualitative Disclosures About Market Risk	9
ITEM 4. Controls and Procedures	9
<b>PART II</b>	
ITEM 1. Legal Proceedings	10
ITEM 1A. Risk Factors	10
ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds	10
ITEM 3. Defaults Upon Senior Securities	10
ITEM 4. Submission of Matters to a Vote of Security Holders	10
ITEM 5. Other Information	10
ITEM 6. Exhibits	10
<b>SIGNATURES</b>	<b>11</b>

SUBAYE, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

	December 31, 2009	September 30, 2009
	(In Thousands)	
	(Unaudited)	(Audited)
<b>Assets</b>		
<b>Current Assets:</b>		
Cash	\$ 2,668	\$ 321
Accounts Receivable, Net of Allowance for Doubtful Accounts of \$363 as of December 31, 2009 and September 30, 2009	13,523	15,706
Prepaid Expenses	3,742	1,902
Deposit for Purchase of Inventoriable Assets	8,147	8,152
Other Current Assets	1,311	1,843
<b>Total Current Assets</b>	<b>29,391</b>	<b>27,924</b>
Property Plant and Equipment, Net of Accumulated Depreciation of \$21,473 and \$20,198 as of December 31, 2009 and September 30, 2009	9,338	10,626
<b>Intangible Assets, Net</b>		
Copyrights, Net of Accumulated Amortization of \$1,738 and \$1,674 as of December 31, 2009 and September 30, 2009	24,386	17,623
Goodwill	557	557
<b>Total Intangible Assets, Net</b>	<b>24,943</b>	<b>18,180</b>
<b>Total Assets</b>	<b>\$ 63,672</b>	<b>\$ 56,730</b>
<b>Liabilities and Equity</b>		
<b>Current Liabilities</b>		
Accounts Payable and Accrued Expenses	\$ 5,906	\$ 4,978
Short Term Debt	2,972	863
<b>Total Current Liabilities</b>	<b>8,878</b>	<b>5,841</b>
<b>Total Liabilities</b>	<b>8,878</b>	<b>5,841</b>
<b>Commitments and Contingencies</b>		
<b>Shareholders' Equity</b>		
Preferred Stock, \$0.001 Par Value, 50,000,000 Shares Authorized, 0 Shares Issued and Outstanding as of December 31, 2009 and September 30, 2009	—	—
Common Stock, \$0.001 Par Value; 150,000,000 Shares Authorized; 6,664,131 and 2,479,243 Shares Issued and Outstanding as of December 31, 2009 and September 30, 2009	7	3
Additional Paid in Capital	48,021	32,452
Deferred Stock Based Compensation	(6,789)	(2,908)

Edgar Filing: SUBAYE, INC. - Form 10-Q

Accumulated Other Comprehensive Income	(27)	54
Retained Earnings	13,582	11,108
Total Shareholders' Equity	54,794	40,709
Noncontrolling Interest in Subsidiaries	-	10,180
Total Equity	54,794	50,889
Total Liabilities and Equity	\$ 63,672	\$ 56,730

The accompanying notes to these consolidated financial statements are an integral part of these balance sheets.

F-1

---

SUBAYE, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
AND OTHER COMPREHENSIVE INCOME

	For the Three Months Ended December 31,	
	2009 (Unaudited)	2008 (Audited)
	(In Thousands, Except Per Share Data)	
Net Sales	\$ 12,714	\$ 9,856
Cost of Sales	7,111	6,139
Gross Profit	5,603	3,717
Operating Expenses		
Advertising	427	108
Other General and Administrative Expenses	1,347	663
Total Operating Expenses	1,774	771
Operating Income	3,829	2,946
Income Tax Expense	(883)	(2)
Net Income	2,946	2,944
Net Income Attributable to the Noncontrolling Interest	(472)	(471)
Net Income Attributable to the Controlling Interest	\$ 2,474	\$ 2,473
Earnings per Common Share		
Basic	\$ 0.47	\$ 1.53
Diluted	\$ 0.47	\$ 1.53
Weighted Average Common Shares Outstanding		
Basic	5,209,013	1,617,627
Diluted	5,231,013	1,617,627
Comprehensive Income		
Net Income	\$ 2,946	\$ 2,944

Other Comprehensive (Loss) Income, Net of Tax			
Foreign Currency Translation Adjustment, Net of Tax		(81)	19
Total Other Comprehensive Income, Net of Tax		2,865	2,963
Comprehensive Income Attributable to the Noncontrolling Interest			
		401	477
Comprehensive Income Attributable to Controlling Interest			
	\$	2,464	\$ 2,486

The accompanying notes to consolidated financial statements are an integral part of these statements.

SUBAYE, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASHFLOWS

	December 31	
	2009	2008
	(In Thousands)	
	(Unaudited)	(Audited)
<b>Cash Flows From Operating Activities:</b>		
Net Income	\$ 2,946	\$ 2,944
<b>Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities—</b>		
Depreciation and Amortization	1,347	1,670
Amortization of Stock Based Compensation	1,040	311
<b>(Increase) Decrease in Assets—</b>		
Accounts Receivable	2,183	(1,196)
Prepaid Expenses	(1,840)	(2,577)
Other Current Assets	532	262
Copyrights	(6,828)	-
<b>Increase (Decrease) in Liabilities —</b>		
Accounts Payable and Accrued Expenses	934	(1,009)
<b>Net Cash Provided By Operating Activities</b>	<b>314</b>	<b>405</b>
<b>Cash Flows From Investing Activities:</b>		
Purchase of Equipment	-	(5)
<b>Net Cash Used in Investing Activities</b>	<b>-</b>	<b>(5)</b>
<b>Cash Flows From Financing Activities:</b>		
Proceeds From Short Term Debt	2,109	123
<b>Net Cash Provided By Financing Activities</b>	<b>2,109</b>	<b>123</b>
Effect of Exchange Rate Changes in Cash	(76)	(32)
<b>Increase in Cash</b>	<b>2,347</b>	<b>491</b>
Cash, Beginning of Period	321	303
Cash, End of Period	\$ 2,668	\$ 794
<b>Supplemental Cash Flow Information:</b>		
<b>Cash Paid During the Period for</b>		
Interest, Net of Amounts Capitalized	\$ —	\$ —
Income Taxes	\$ 6	\$ 2
<b>Supplemental Schedule of Noncash Investing and Financing Activities:</b>		
Issuance of Stock for Services, Deferred Compensation	\$ 4,920	\$ 350
Adjustment of additional paid-in-capital and non-controlling interests from investment in Subaye Inc, by non-controlling interests	\$ 10,652	\$ -

The accompanying notes to consolidated financial statements are an integral part of these statements.



F-3

---

SUBAYE, INC. AND SUBSIDIARIES  
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE THREE MONTHS ENDED DECEMBER 31, 2009 AND 2008

NOTE 1 - BUSINESS DESCRIPTION AND ORGANIZATION

Subaye, Inc., a Delaware corporation (together with its consolidated subsidiaries, “Subaye” or the “Company”) is a leading video advertising and entertainment media provider in China. Subaye’s platform includes production, upload, storage, sharing and publishing onto more than 33 main video sharing portal websites. Subaye also offers SaaS business solutions and is in the process of developing what Subaye believes is the first online shopping mall in the world that will utilize 3D imaging throughout the online customer interface. Subaye’s video sharing services, SaaS solutions and its online shopping mall will be fully integrated in 2010. Subaye’s members will use Subaye’s SaaS online content management software to manage their online video and graphic showcases, maintain customer data and to manage operations within their webshops at the online shopping mall. Subaye utilizes its experience and contacts within the entertainment media industry in Asia to produce and place advertisements on behalf of its customers. The Company also routinely invests the Company’s funds in entertainment productions in Asia. Typically, these investments consist of the purchase of the full or partial copyrights to an entertainment production. Subaye’s trade services are offered to customers based in Asia, North America and Europe. These customers order products through Subaye and ship products both domestically within China and internationally. Subaye’s trade services provide solutions for both importing and exporting transactions.

On October 26, 2009, the Company changed its name to Subaye, Inc. The Company's common stock continues to be quoted under the symbol, “SBAY.OB,” on the FINRA over-the-counter bulletin board (“OTCBB”) in the United States of America.

The Company operates in three distinct business segments:

1. Online Membership Services - The Company provides online content and member services for commercial use.
2. Entertainment Media - The Company produces and places advertising solutions on behalf of its customers and routinely invests in entertainment arts productions in China.
3. Trade Services – The Company operates a domestic and international importing and exporting services operation to acquire and distribute goods within China or internationally.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The condensed consolidated financial statements, prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”), include the assets, liabilities, revenues, expenses and cash flows of the Company and all its subsidiaries. This basis of accounting differs in certain material respects from that used for the preparation of the books and records of the Company’s principal subsidiaries, which are prepared in accordance with the accounting principles and the relevant financial regulations applicable to enterprises with limited liabilities established in China the accounting standards used in the place of their domicile. The accompanying consolidated financial statements reflect necessary adjustments not recorded in the books and records of the Company’s subsidiaries to present them in conformity with GAAP.

Subsidiaries	Countries Registered In	Percentage of Ownership
MyStarU Ltd.	Hong Kong, The People’s Republic of China	100.00%
3G Dynasty Inc.	British Virgin Islands	100.00%

Edgar Filing: SUBAYE, INC. - Form 10-Q

Guangzhou Panyu Metals & Materials Limited	The People's Republic of China	100.00%
Subaye.com *	United States of America, Delaware	100.00%
Subaye IIP Limited *	British Virgin Islands	100.00%
Guangzhou Subaye Computer Tech Limited *	The People's Republic of China	100.00%
Media Group International Limited *	Hong Kong, The People's Republic of China	100.00%

\*On November 6, 2009, the Company entered into a Share Exchange Agreement with certain shareholders of its subsidiary, Subaye.com, Inc. Pursuant to the terms of the Share Exchange, the Company issued 3,408,852 shares of its common stock in exchange for all outstanding shares of common stock of Subaye.com, Inc. the Company did not already own (the "Share Exchange"). As a result of the Share Exchange, Subaye.com, Inc., and the wholly-owned subsidiaries of Subaye.com, Inc., effectively became wholly-owned subsidiaries of the Company.

F-4

---

The accompanying unaudited consolidated financial statements have been prepared in accordance with GAAP for interim financial information and with the instructions to Form 10-Q. They do not include all of the information and footnotes required by GAAP for a complete financial presentation. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation, have been included in the accompanying unaudited condensed consolidated financial statements. Operating results for the periods presented are not necessarily indicative of the results that may be expected for the full year. The Company's accounting policies and certain other disclosures are set forth in the notes to the consolidated financial statements contained in the Company's Annual Report on Form 10-K for the year ended September 30, 2009 as filed with the United States Securities and Exchange Commission on December 29, 2009. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and notes thereto. The preparation of condensed consolidated financial statements in conformity with 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 date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Financial Accounting Standards Board's Accounting Standards Codification ("ASC") became the sole source of GAAP as of September 15, 2009. References to the ASC are made throughout this Form 10-Q and refer to specific sections of the ASC in relation to the topics referenced within this Form 10-Q.

Adoption of ASC 810-10-65, Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB 51 ("ASC 810-10-65")

The adoption of ASC 810-10-65 did not have a material effect on the Company's financial condition, results of operations or cash flows for the three months ended December 31, 2009 and 2008, respectively, or as of December 31, 2009 and September 30, 2009, respectively. However, as a result of the retrospective presentation and disclosure requirements of ASC 810-10-65, the adoption of ASC 810-10-65 did affect the presentation and disclosure of noncontrolling interests and basic and diluted earnings per common share in the Company's condensed consolidated financial statements for the three months ended December 31, 2008 and as of September 30, 2009, respectively.

ASC 810-10-65 establishes new standards that govern the accounting for and reporting of (1) noncontrolling interest in partially owned consolidated subsidiaries and (2) the loss of control of subsidiaries. Significant changes to the accounting for noncontrolling interests include (a) the inclusion of noncontrolling interests in the equity section of the controlling entity's condensed consolidated balance sheet rather than in the mezzanine section and (b) the requirement that changes in the controlling entity's interest in the noncontrolling interest, without a change in control, be recognized in the controlling entity's equity rather than being accounted for by the purchase method, which accounting under the purchase method would have given rise to goodwill.

The Company has owned a majority interest of its subsidiary, Subaye.com, Inc., since June 2006. The principal effect of the adoption of ASC 810-10-65 on the September 30, 2009 condensed consolidated balance sheet was to reclassify the noncontrolling interest of \$10,180 thousand from the mezzanine section of the balance sheet to stockholders' equity attributable to noncontrolling interest, thus increasing the total of the condensed consolidated stockholders' equity by that amount, as follows:

	September 30, 2009 (000's)
Equity, as Previously Reported	\$ 40,709
Increase for ASC 810-10-65 Reclassification of Non-Controlling Interest	10,180

Equity, as Adjusted	\$ 50,889
---------------------	-----------

Additionally, the adoption of ASC 810-10-65 requires that net income, as previously reported prior to the adoption of ASC 810-10-65, be adjusted to include the net income attributable to the noncontrolling interest, and that a new separate caption for net income attributable to common shareholders be presented in the condensed consolidated statements of operations. Thus, after the adoption of ASC 810-10-65, condensed consolidated net income increases by \$471 thousand for the three months ended December 31, 2008.

ASC 810-10-65 also requires similar disclosure regarding comprehensive income. Therefore, after the adoption of ASC 810-10-65 condensed consolidated comprehensive income increases by \$471 for the three months ended December 31, 2008

#### Revenue Recognition

##### Online Membership Services - Monthly Website Subscriptions

Revenue for the monthly subscription from the members who subscribed to the Company's websites is recognized on a pro-rata basis, is calculated on a day-to-day basis and invoiced at the end of each month of full service in accordance under the relevant sections of the ASC, namely ASC Topic 605 "Revenue Recognition" ("ASC 605"). The Company does not currently charge a cancellation fee or penalty if and when a customer decides to terminate their membership with our websites.

F-5

---

Current terms of the www.subaye.com membership agreement stipulate that the customer pays a nonrefundable fee of approximately \$120 per month for access to the marketing and advertising capabilities in place at www.subaye.com. The Company does also providers SaaS software to its members, although, SaaS software contracts are entered into separately and in addition to the regular membership agreement.

Subaye.com entered into agreements with two merchant service providers on October 2, 2009. The merchant service providers have two tasks: (i) to assist the members of www.subaye.com in preparing each member's corporate branding video, which is to be uploaded to www.subaye.com and (ii) to assist Subaye.com with the daily operations of www.subaye.com and more specifically, to collect the monthly member fees, which are currently paid in cash, from the members of www.subaye.com. Collecting these cash receipts, tracking which customers have paid and which have not, and remitting the cash to the Company, is a time intensive project each month. Subaye.com has never experienced collection issues and does not expect any collection issues to occur in the future. The merchant service providers were compensated with a total of 320,000 shares of the Company's common stock valued at \$2,560 thousand on October 2, 2009. Each agreement is for a term of three years. The Company amortizes the compensation provided to these merchant service providers over the three year term and records its revenues net of this stock compensation paid to the merchant service providers, in accordance with ASC 605-45. The Company believes net revenue presentation is reasonable given that it shares the obligation to perform with these merchant service providers with regard to its membership contracts with its customers.

#### Advertising Costs

The Company expenses advertising costs as the costs are incurred in accordance with ASC 720-35 "Advertising Costs".

#### Reclassifications

Certain reclassifications to the Company's condensed consolidated balance sheets and condensed consolidated statements of operations and other comprehensive income have been made to the September 30, 2009 and December 31, 2008 financial statements to conform to the presentation of these financial statements. These reclassifications did not impact the Company's total assets, liabilities, net income or total equity for the three months ended December 31, 2009 and 2008 and as of September 30, 2009, respectively.

#### NOTE 3 - ACCOUNTS RECEIVABLE

The Company's business operations are conducted in China. During the normal course of business, the Company extends unsecured credit to its customers. Management reviews its accounts receivable on a regular basis to determine if the allowance for doubtful accounts is adequate. An estimate for doubtful accounts is made when collection of the full amount is no longer probable. The Company has not experienced significant difficulty in collecting its accounts receivable in the past and is has no reason to believe this may change in the near future.

Trade accounts receivable at December 31, 2009 and September 30, 2009 consisted of the following:

	December 31, 2009 (000's)	September 30, 2009 (000's)
Trade Accounts Receivable	\$ 13,886	\$ 16,069
Less: Allowance for Doubtful Accounts	(363)	(363)
Totals	\$ 13,523	\$ 15,706

The activity in the allowance for doubtful accounts for trade accounts receivable as of December 31, 2009 and September 30, 2009 is as follows:

	December 31, 2009 (000's)	September 30, 2009 (000's)
Beginning Allowance for Doubtful Accounts	\$ 363	\$ 31
Additional Charge to Bad Debt Expense	-	332
Ending Allowance for Doubtful Accounts	\$ 363	\$ 363

The Company has the following concentrations of business with customers constituting greater than 5% of the Company's gross accounts receivable as of December 31, 2009 and September 30, 2009. The nonpayment of these accounts receivables, individually or in the aggregate, could have a material impact on our future results of operations.

These accounts receivable totaled \$9,581 thousand and \$12,534 thousand or 69% and 78% of our gross total accounts receivable as of December 31, 2009 and September 30, 2009, respectively.

	December 31, 2009	September 30, 2009
Customer 1	37%	36%
Customer 2	12%	16%
Customer 3	15%	6%
Customer 4	-%	20%
Customer 5	5%	-%

#### NOTE 4 – DEPOSIT FOR INVENTORIABLE ASSETS

On May 3, 16 and 26, 2009, the Company's subsidiary, Subaye IIP Limited, entered into three agreements with three consumer goods distributors in China. The products will include clothes, footwear, bags and garniture, jewelry and electronics. The consumer goods distributors committed to delivering goods ordered by Subaye IIP Limited or the members of www.subaye.com "just in time." If the consumer goods distributors do not deliver the products ordered by the first day subsequent to the order, the consumer goods distributors will pay Subaye IIP Limited a penalty equal to 5% of the cost of the product ordered per day it is delivered late. The contracts are valid from May 3, 16 and 26, 2009 through November 2, 15 and 25, 2010, respectively. In accordance with the contract, Subaye IIP Limited paid a deposit of \$8,152 thousand. The deposit will be used by the consumer goods distributor to ensure product is available for ordering by Subaye IIP Limited or the members of www.subaye.com on an as needed basis.

#### NOTE 5 - PROPERTY AND EQUIPMENT, NET

Property and equipment consisted of the following:

	December 31, 2009 (000's)	September 30, 2009 (000's)
Computer Software & Equipment	\$ 14,499	\$ 14,504
Websites	16,167	16,175
Motor Vehicle	84	84
Furniture & Fixtures	61	61
	30,811	30,824
Less: Accumulated depreciation and amortization	(21,473)	(20,198)
	\$ 9,338	\$ 10,626

#### NOTE 6 - GOODWILL & INTANGIBLE ASSETS

Intangible assets are stated at cost (estimated fair value upon contribution or acquisition), less accumulated amortization and impairment.

The following table summarizes the carrying values of all the Company's goodwill and intangible assets by category, as of December 31, 2009 and September 30, 2009:

December 31, 2009 (000's)	September 30, 2009 (000's)
---------------------------------	----------------------------------



Edgar Filing: SUBAYE, INC. - Form 10-Q

Copyrights - Motion Picture, Television, Internet and DVD Productions	\$	26,124	\$	19,297
Accumulated Amortization		(1,738)		(1,674)
Copyrights, Net		24,386		17,623
Goodwill		557		557
Total	\$	24,943	\$	18,180

The following table summarizes the copyrights held by the Company as of December 31, 2009, all of which are or will be PRC productions or are being held for investment purposes. All copyrights are wholly-owned by the Company unless noted otherwise.

F-7

---

Copyrights for Movies, DVDs, Television and Internet Broadcasting

Big Movie: Subaye \*

DaYouCun

PaoBu

True?

Big Future

Qianfu

Valleys and Peaks Tactics

\*The copyright for “Big Movie: Subaye” does not include rights for television broadcasting.

Copyrights for Internet Broadcasting Only

Big Movie 2: Two Stupid Eggs

The Company amortizes its copyrights using the individual-film-forecast-computation method, in accordance with ASC 926, which amortizes or accrues (expenses) such costs in the same ratio that current period actual revenue (numerator) bears to estimated remaining unrecognized ultimate revenue as of the beginning of the current fiscal year (denominator). Total amortization of the copyrights was \$65 thousand and \$115 thousand for the three months ended December 31, 2009 and 2008, respectively, and was included in cost of sales.

The ultimate revenue to be included in the denominator of the individual-film-forecast-computation method fraction is subject to certain limitations as set forth in ASC 926. If an event or change in circumstance indicates that the Company should assess whether the fair value of the copyright is less than its unamortized costs, the Company will determine the fair value of the film and will write off the amount by which the unamortized capitalized costs exceeds the episode's fair value. Accordingly, the Company cannot subsequently restore any amounts written off in previous fiscal years to income.

Given the environment in which the Company currently operates, it is reasonably possible that management's estimate of the economic useful lives of these assets or the assumption that they will recover their carrying amounts from future operations, could change in the future.

Intangible assets of the Company are reviewed annually or more often if circumstances dictate, to determine whether their carrying value has become impaired. The Company considers assets to be impaired if the carrying value exceeds the future projected cash flows from related operations. The Company also re-evaluates the periods of amortization to determine whether subsequent events and circumstances warrant revised estimates of useful lives. As of December 31, 2009 and September 30, 2009, respectively, the Company expects these assets, at their current carrying value, to be fully recoverable.

NOTE 7 – DEPRECIATION AND AMORTIZATION

The Company's depreciation and amortization recorded within these financial statements is significant and is related to the Company's copyrights, websites and software, respectively. Below is a table outlining depreciation and amortization for each asset class which is included in costs of goods sold or operating expenses for each period presented within the financial statements.

Three Months Ended December	
31,	
2009	2008

Edgar Filing: SUBAYE, INC. - Form 10-Q

	(000's)	(000's)
Depreciation Included in Operating Expenses	\$ 5	\$ 7
Amortization of Copyrights Included Within Cost of Sales	65	115
Amortization of Websites Included Within Cost of Sales	494	764
Amortization of Software Included Within Cost of Sales	783	784
Total Depreciation and Amortization	\$ 1,347	\$ 1,670

F-8

---

## NOTE 8 - SHORT TERM DEBT

Total debt obligations as of December 31, 2009 and September 30, 2009 consisted of the following:

	December 31, 2009 (000's)	September 30, 2009 (000's)
5.10% Bank Loan, Due on Demand	\$ 863	\$ 863
1.40% ICBC Bank Loans, Due October 10, 2010	1,385	-
1.16% ICBC Bank Loans, Due November 30, 2010	724	-
	2,972	
<b>Total Debt Obligations</b>		
Less: Current Maturities	2,972	863
<b>Total Long-Term Debt</b>	<b>\$ -</b>	<b>\$ -</b>

## Bank Loans

On September 19, 2008, the Company entered into a bank loan with Panyu RuralCredit Union and Cooperative Bank for a total of \$1,021 thousand (7,000,000 Reminbi). The bank loan had an annualized interest rate of 8.64% with interest payable on a monthly basis. The Company used the net proceeds from the bank loan to invest in computer equipment and computer software and for other general corporate purposes. As of December 31, 2009, the outstanding borrowings totaled \$863 thousand. The interest rate has decreased to 5.10% per annum. The bank loan and all unpaid interest is payable in full on demand.

On October 19, 2009, the Company entered into two additional bank loans totaling \$1,385 thousand with Industrial and Commercial Bank of China ("ICBC"). These bank loans both mature on October 19, 2010 and carry interest at approximately 1.40% per annum.

On November 30, 2009, the Company entered into a bank loan totaling \$724 thousand with ICBC. The bank loan matures on November 30, 2010 and carries interest at approximately 1.16% per annum.

Aggregate scheduled maturities of our debt obligations for each of the five 12- month periods subsequent to December 31, 2009, and thereafter are as follows, in thousands:

12 Months Ended December 31,	
2010	\$ 2,972
2011	-
2012	-
2013	-
2014	-
Subsequent to 2014	-
<b>Total Scheduled Debt Payments</b>	<b>\$ 2,972</b>

## NOTE 9 - STOCKHOLDERS' EQUITY

The Company is authorized to issue 200,000,000 shares, in aggregate, consisting of 150,000,000 shares of common stock, \$0.001 par value, and 50,000,000 shares of preferred stock, \$0.001 par value. The Company's Certificate of

Incorporation authorizes the Board of Directors (the "Board") to determine the preferences, limitations and relative rights of any class or series of Company preferred stock prior to issuance and each such class or series must be designated with a distinguishing designation prior to issuance. As of December 31, 2009, no shares of the Company's preferred stock and 6,664,131 shares of the Company's common stock were issued and outstanding.

On October 23, 2009, the Company effectuated a reverse stock split on a 100 to 1 (100:1) basis.

On November 6, 2009, the Company entered into a Share Exchange Agreement (the "Share Exchange") with certain shareholders of its subsidiary, Subaye.com, Inc. Pursuant to the terms of the Share Exchange, the Company issued 3,408,852 shares of its common stock in exchange for all outstanding shares of common stock of Subaye.com, Inc. the Company did not already own.

#### Stock-Based Compensation

On July 16, 2007, the Company agreed to issue 3,650 shares of common stock to a consultant for international business consulting services at price of \$16.00 per share for a total consideration equal to \$58 thousand. The shares are being amortized over 24 months with stock-based compensation expense of \$2 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$0 and \$7 thousand, respectively.

On October 3, 2007, the Company issued 7,350 shares of common stock to the Company's Chief Financial Officer for services to be provided over a two year period at price of \$13.00 per share for a total consideration equal to \$96 thousand. The shares are being amortized over 24 months with stock-based compensation expense of \$4 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$0 and \$12 thousand, respectively.

On October 3, 2007, the Company issued 10,000 shares of common stock to the Company's Chief Executive Officer for services to be provided over a two year period at price of \$13.00 per share for a total consideration equal to \$130 thousand. The shares are being amortized over 24 months with stock-based compensation expense of \$5 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$0 and \$16 thousand, respectively.

On October 3, 2007, the Company issued 4,000 shares of common stock to an investor relations consultant, for services to be provided over a 24 month period at price of \$13.00 per share for a total consideration equal to \$52 thousand. The shares are being amortized over 24 months with stock-based compensation expense of \$2 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$0 and \$6 thousand, respectively.

On September 18, 2008, the Company agreed to issue 3,500 shares of common stock to Mary Kratka for investor relations and promotions services at price of \$8.00 per share for total consideration equal to \$28 thousand. The shares are being amortized over approximately 3 months with a stock-based compensation expense of \$9 thousand each month. The total stock-based compensation expense for for the three months ended December 31, 2009 and December 31, 2008 was \$0 and \$26 thousand, respectively.

On October 10, 2008, the Company agreed to issue 70,000 shares of common stock to Results Group International for consulting services at a price of \$5.00 per share for total consideration equal to \$350 thousand. The shares are being amortized over 36 months with a stock-based compensation expense of \$10 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$39 thousand and \$26 thousand, respectively.

On January 6, 2009, the Company agreed to issue 80,000 shares of common stock to Bloomen Limited for consulting services over a 36-month contract at a price of \$4.00 per share for total consideration equal to \$320 thousand. The shares are being amortized over 36 months with a stock-based compensation expense of \$9 thousand each month. The total stock-based compensation for the three months ended December 31, 2009 and December 31, 2008 was \$25 thousand and \$0, respectively.

On March 30, 2009, the Company agreed to issue 85,000 shares of common stock to Trueboon Limited for consulting services over a 36 month contract at a price of \$6.00 per share for total consideration equal to \$510 thousand. The shares are being amortized over 36 months with a stock-based compensation expense of \$14 thousand each month, commencing in April 2009. The total stock-based compensation expense as of December 31, 2009 and September 30, 2009 was \$100 thousand and \$14 thousand and \$0, respectively.

On September 18, 2009, the Company agreed to issue 20,000 shares of common stock to Virtrius Limited, an entity wholly-owned by the Company's Chief Financial Officer, for marketing and investor relations services at price of \$9.00 per share for total consideration equal to \$180 thousand. The shares are being amortized over approximately 6 months with a stock-based compensation expense of \$30 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$91 thousand and \$0, respectively.

On September 24, 2009, the Company agreed to issue 120,000 shares of common stock to China Industry Park Holdings Limited, for consulting services related to the IPTV industry in China at a price of \$9.10 per share for total consideration equal to \$1,092 thousand. The shares will be amortized over the term of the agreement beginning on October 1, 2009 for approximately 36 months with a stock-based compensation expense of \$30 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$98 thousand and \$0, respectively.

On September 24, 2009, the Company agreed to issue 20,000 shares of common stock to its President for a two year employment agreement at a price of \$9.10 per share for total consideration equal to \$182 thousand. The shares will be amortized over approximately 24 months with a stock-based compensation expense of \$8 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$23 thousand and \$0, respectively.

On September 24, 2009, the Company agreed to issue 30,000 shares of common stock to its Chief Executive Officer for a two year employment agreement at a price of \$9.10 per share for total consideration equal to \$273 thousand. The shares will be amortized over approximately 24 months with a stock-based compensation expense of \$11 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$34 thousand and \$0, respectively.

On October 2, 2009, the Company agreed to issue 200,000 shares of common stock to a merchant service provider for a three year consulting agreement at a price of \$8.00 per share for total consideration equal to \$1,600 thousand. The shares will be amortized over approximately 36 months with a stock-based compensation expense of \$44 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$132 thousand and \$0, respectively.

On October 2, 2009, the Company agreed to issue 120,000 shares of common stock to a merchant service provider for a three year employment agreement at a price of \$8.00 per share for total consideration equal to \$960 thousand. The shares will be amortized over approximately 36 months with a stock-based compensation expense of \$27 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$79 thousand and \$0, respectively.

On October 2, 2009, the Company agreed to issue 7,500 shares of common stock to its new Vice President for a two year employment agreement at a price of \$8.00 per share for total consideration equal to \$60 thousand. The shares will be amortized over approximately 24 months with a stock-based compensation expense of \$2 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$7 thousand and \$0, respectively.

On October 11, 2009, the Company agreed to issue 22,500 shares of common stock to its Chief Financial Officer for a three year employment agreement at a price of \$11.50 per share for total consideration equal to \$259 thousand. The shares will be amortized over approximately 36 months with a stock-based compensation expense of \$7 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$19 thousand and \$0, respectively.

On November 9, 2009, the Company agreed to issue 30,000 shares of common stock to a marketing and investor relations consultant at a price of \$12.12 per share for total consideration equal to \$364 thousand. The shares will be amortized over approximately 24 months with a stock-based compensation expense of \$15 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$26 thousand and \$0, respectively.

On November 9, 2009, the Company agreed to issue 48,000 shares of common stock to a business development consultant at a price of \$12.12 per share for total consideration equal to \$582 thousand. The shares will be amortized over approximately 24 months with a stock-based compensation expense of \$24 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$41 thousand and \$0, respectively.

On November 9, 2009, the Company agreed to issue 48,000 shares of common stock to a business development consultant at a price of \$12.12 per share for total consideration equal to \$582 thousand. The shares will be amortized over approximately 24 months with a stock-based compensation expense of \$24 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$41 thousand and \$0, respectively.

On November 17, 2009, the Company agreed to issue 34,800 shares of common stock to its three new independent members of the Board of Directors at a price of \$15.50 per share for total consideration equal to \$539 thousand. The shares will be amortized over approximately 12 months with a stock-based compensation expense of \$45 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$80 thousand and \$0, respectively.

#### Subaye.com Stock Based Compensation

On October 1, 2007, Subaye.com issued 170,000 shares of common stock to Subaye.com's Chief Executive Officer for services to be provided over a two year period from January 2, 2008 through December 31, 2009 at a price of \$2.00 per share for a total consideration equal to \$340 thousand. The shares will be amortized over 24 months with stock-based compensation expense of \$14 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$43 thousand and \$43 thousand, respectively.

On October 1, 2007, Subaye.com issued 50,000 shares of common stock to an employee of Subaye.com for services to be provided beginning January 1, 2008 at a price of \$2.00 per share for a total consideration equal to \$100 thousand. The shares will be amortized over 24 months with stock-based compensation expense of \$4 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$12 thousand and \$12 thousand, respectively.

On January 2, 2008, Subaye.com agreed to issue 450,000 shares of common stock to an investor relations consultant, for services to be provided over a 24 month period from January 2, 2008 through December 31, 2009 at price of \$2.00 per share for a total consideration equal to \$900 thousand. The shares will be amortized over 24 months with stock-based compensation expense of \$38 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$113 thousand and \$113 thousand, respectively.



On January 2, 2008, Subaye.com issued 50,000 shares of common stock to an executive, for services to be provided over a 24 month period at price of \$2.00 per share for a total consideration equal to \$100 thousand. The shares will be amortized over 24 months with stock-based compensation expense of \$4 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$12 thousand and \$12 thousand, respectively.

On January 2, 2008, Subaye.com issued 70,800 shares of common stock to an executive, for services to be provided over a 24 month period at price of \$2.00 per share for a total consideration equal to \$142 thousand. The shares will be amortized over 24 months with stock-based compensation expense of \$6 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$18 thousand and \$18 thousand, respectively.

On February 26, 2008, Subaye.com issued 78,425 shares of common stock to its Chief Financial Officer, for services to be provided over a 24 month period at price of \$2.00 per share for a total consideration equal to \$157 thousand. The shares will be amortized over 24 months with stock-based compensation expense of \$7 thousand each month. The total stock-based compensation expense for the three months ended December 31, 2009 and December 31, 2008 was \$7 thousand and \$20 thousand, respectively.

Total stock compensation expense reported was \$1,040 thousand and \$311 thousand for the three months ended December 31, 2009 and 2008, respectively.

## NOTE 10 – NONCONTROLLING INTEREST

On November 6, 2009, the Company entered into a Share Exchange Agreement with certain shareholders of its subsidiary, Subaye.com, Inc. Pursuant to the terms of the Share Exchange, the Company issued 3,408,852 shares of its common stock in exchange for all outstanding shares of common stock of Subaye.com, Inc. the Company did not already own. As a result of the Share Exchange, Subaye.com, Inc., and each of the wholly-owned subsidiaries of Subaye.com, Inc., effectively became a wholly-owned subsidiaries of the Company. The transaction was accounted for as a change in the ownership interests of the Company with an entity under common control, in accordance with ASC 810-10-65. As a result, the value of the 3,408,852 shares issued to consummate the Share Exchange Agreement was \$10,652 thousand, which represented the historical cost basis of the balance of the net assets acquired through the Share Exchange Agreement, which included significant assets as well as liabilities owed to the Company. The following disclosure provides details regarding the change in the noncontrolling ownership interests of the Company's subsidiaries, in accordance with ASC 810-10-55-4.

Net Income Attributable to Subaye, Inc. and Transfers to  
and from the Noncontrolling Interest

	For the Three Months Ended December 31,	
	2009 (000's)	2008 (000's)
Net Income Attributable to Subaye, Inc.	\$ 472	\$ 471
Transfers (to) from the Noncontrolling Interest		
Increase in Subaye, Inc.'s Additional Paid in Capital for the Issuance of 3,408,852 Shares of Common Stock to the Shareholders of the Noncontrolling Interest	(10,652)	-
Change from Net Income Attributable to Subaye, Inc. and Transfers (to) from the Noncontrolling Interest	\$ (10,180)	\$ 471

## NOTE 11 - INCOME TAX

## United States of America

Since the Company had no operations within the United States, there is no provision for United States taxes and there are no deferred tax amounts for the three months ended December 31, 2009 and December 31, 2008 respectively.

## Delaware

The Company and its subsidiary, Subaye.com, are incorporated in Delaware but do not conduct business in Delaware. Therefore, the Company is not subject to corporate income tax.

## British Virgin Islands

3G Dynasty and Subaye IIP are incorporated in the British Virgin Islands and, under the current laws of the British Virgin Islands, are not subject to income taxes.

## Hong Kong

Media Group International Ltd. and MyStarU Ltd. are incorporated in Hong Kong and are subject to Hong Kong taxation on its activities conducted in Hong Kong and income arising in or derived from Hong Kong. No provision for Hong Kong profits tax has been made as the Company's Hong Kong subsidiaries incurred a loss during the three months ended December 31, 2009 and 2008, respectively. The applicable Hong Kong statutory tax rate as of December 31, 2009 and September 30, 2009 was 17.5%, respectively.

#### People's Republic of China

Enterprise income tax in PRC is generally charged at 25% of a company's assessable profit, of which 22% is a national tax and 3% is a local tax. The Company's subsidiaries incorporated in the PRC, namely Guangzhou Subaye and Panyu M&M, are subject to PRC enterprises income tax at the applicable tax rates on the taxable income as reported in their Chinese statutory accounts in accordance with the relevant enterprises income tax laws applicable to foreign enterprises. Pursuant to the same enterprises income tax laws, the Company's subsidiaries are fully exempted from PRC enterprises income tax for two years starting from the first profit-making year, followed by a 50% tax exemption for the next three years.

No provision for enterprise income tax in the PRC had been made for the years ended September 30, 2009 and 2008 due to the fact that the Company was exempt from PRC tax based on the statutory provisions granting a tax holiday for a two year period, as stated above for the years ended September 30, 2009 and 2008 respectively.

The Company is governed by the Income Tax Law of the People's Republic of China concerning Foreign Investment Enterprises and Foreign Enterprises and various local income tax laws ("the Income Tax Laws"). Under the Income Tax Laws, foreign investment enterprises ("FIE") generally are subject to an income tax at an effective rate of 25% on income as reported in their statutory financial statements after appropriate tax adjustments unless the enterprise is located in specially designated regions of cities for which more favorable effective tax rates apply. Upon approval by the PRC tax authorities, FIEs scheduled to operate for a period of 10 years or more and engaged in manufacturing and production may be exempt from income taxes for two years, commencing with their first profitable year of operations, after taking into account any losses brought forward from prior years, and thereafter with a 50% exemption for the next three years.

Beginning January 1, 2008, the new Enterprise Income Tax (“EIT”) law of the People’s Republic of China replaced the existing laws for Domestic Enterprises (“DES”) and FIEs.

The key changes are:

- a. The new standard EIT rate of 25% will replace the 33% rate currently applicable to both DES and FIEs, except for “high tech companies” who pay a reduced rate of 15%. The Company currently believes it will qualify as a high tech company under the rule.
- b. Companies established before March 16, 2007 will continue to enjoy tax holiday treatment approved by local government for a grace period of the next five years or until the tax holiday term is completed, whichever is sooner.

The Company and all of its subsidiaries, except for Subaye IIP, were established before March 16, 2007. Subaye IIP is a British Virgin Islands entity and is 100% owned by the Company. Subaye IIP is therefore treated as a pass-through entity for PRC tax purposes and is therefore not subject to PRC taxes.

The provision for enterprise income tax in the PRC is \$883 thousand for the three months ended December 31, 2009. No provision for enterprise income tax in the PRC had been made the three months ended December 31, 2008 due to the fact that certain subsidiaries of the Company are exempt from PRC tax based on the statutory provisions granting a tax holiday for a two year period, as stated above, specifically for the years ended September 30, 2009 and 2008, respectively. The Company’s PRC tax holiday expired on October 1, 2009. The following table details the aggregate effect of the tax holiday on the Company’s results of operations.

	December 31, 2009 (000’s)	December 31, 2008 (000’s)
PRC Tax Without Consideration of Tax Holiday	\$ 883	\$ 736
PRC Tax Savings as a Result of Tax Holiday	\$ -	\$ (736)
Increase in Basic and Diluted Earnings Per Share as a Result of Tax Holiday	\$ -	\$ 0.45

The following table reconciles the U.S. statutory rates to the Company’s effective tax rate for the three months ended December 31, 2009 and December 31, 2008:

	2009	2008
U.S. Statutory Rates	35.0%	35.0%
Foreign Income	(35.0)%	(35.0)
China and Hong Kong Tax Rates, Blended Effective Rate	18.0%	25.0
China Income Tax Exemption	.0%	(25.0)
Effective Income Tax Rates	18%	0%

#### Value Added Tax

Enterprises or individuals who sell products, engage in repair and maintenance or import and export goods in the PRC are subject to a value added tax in accordance with Chinese laws. The value added tax rate applicable to the Company is 6% of the gross sales price. No credit is available for VAT paid on the purchases.

#### NOTE 12 - COMMITMENTS & CONTINGENCIES

##### Operating Leases

In the normal course of business, the Company leases office space under operating lease agreements. The Company rents office space, primarily for regional sales administration offices, in commercial office complexes that are conducive to administrative operations. The operating lease agreements generally contain renewal options that may be exercised at the Company's discretion after the completion of the base rental terms. In addition, many of the rental agreements provide for regular increases to the base rental rate at specified intervals, which usually occur on an annual basis.

On July 1, 2008, the Company entered into a lease for new office space in Foshan City, Guangdong, China for approximately \$5 thousand per month through June 30, 2011.

F-13

---

On February 1, 2009, the Company entered into a lease agreement to utilize approximately 22,000 square feet of office space at 349 Dabei Road, Shiqiao Street, Panyu District, Guangzhou City, Guangdong, China 511400 for approximately \$9 thousand per month through January 31, 2011.

The following table summarizes the Company's future minimum lease payments under operating lease agreements for the five years subsequent to December 31, 2009 in thousands:

Twelve Months Ended December 31,		
	2010	\$ 164
	2011	37
		\$ 201

The Company recognizes lease expense on a straight-line basis over the life of the lease agreement. Contingent rent expense is recognized as it is incurred. Total rent expense in continuing operations from operating lease agreements was \$42 thousand and \$306 thousand for the three months ended December 31, 2009 and 2008, respectively.

#### Contingent Stock Issuance

On September 18, 2009, the Company entered into a six month consulting agreement with an entity wholly-owned by the Company's Chief Financial Officer. In accordance with the terms of the consulting agreement, if during the term of the consulting agreement, the Company successfully obtains a listing on a stock exchange such as the NASDAQ Global Market, NASDAQ Capital Market, NASDAQ Global Select or NYSE Amex, the entity will be awarded a stock issuance of 10,000 shares of common stock. As of February 12, 2010 the Company has applied for a listing on the NASDAQ Global Market but has not yet received approval for the listing.

#### Litigation

We may be involved from time to time in ordinary litigation that will not have a material effect on our operations or finances. We are not aware of any pending or threatened litigation against the Company or our officers and directors in their capacity as such that could have a material impact on our operations or finances.

#### NOTE 13 - OPERATING RISK

##### Credit risk

The Company is exposed to credit risk from its cash at bank and fixed deposits and bills and accounts receivable. The credit risk on cash at bank and fixed deposits is limited because the counterparties are recognized financial institutions. Bills and accounts receivable are subjected to credit evaluations. An allowance has been made for estimated irrecoverable amounts which has been determined by reference to past default experience and the current economic environment.

##### Foreign currency risk

Most of the transactions of the Company were settled in Renminbi and U.S. dollars. In the opinion of the directors, the Company does not have significant foreign currency risk exposure.

Company's operations are substantially in foreign countries

Substantially all of the Company's products are manufactured in China. The Company's operations are subject to various political, economic, and other risks and uncertainties inherent in China. Among other risks, the Company's operations are subject to the risks of restrictions on transfer of funds; export duties, quotas, and embargoes; domestic and international customs and tariffs; changing taxation policies; foreign exchange restrictions; and political conditions and governmental regulations.

NOTE 14 - SEGMENT REPORTING

The Company operates in three distinct business segments:

1. Online Membership Services - The Company provides online content and member services for commercial use.
2. Entertainment Media - The Company produces and places advertising solutions on behalf of its customers and routinely invests in entertainment arts productions in the PRC
3. Trade Services – The Company operates a domestic and international importing and exporting services operation to acquire and distribute goods within the PRC or internationally.

Edgar Filing: SUBAYE, INC. - Form 10-Q

Three Months Ended December 31, 2009 (Unaudited)	Online Membership Services (000's)	Trade Services (000's)	Entertainment Media (000's)	Consolidated Total (000's)
Net Sales	\$ 6,912	\$ 4,255	\$ 1,547	\$ 12,714
Cost of Sales	1,427	4,133	1,551	7,111
Segment Income	4,607	18	(1,679)	2,946
Segment Assets	27,591	6,708	29,373	63,672
Expenditures for Segment Assets	\$ -	\$ -	\$ 6,828	\$ 6,828

Three Months Ended December 31, 2008 (Unaudited)	Online Membership Services (000's)	Trade Services (000's)	Entertainment Media (000's)	Consolidated Total (000's)
Net Sales	\$ 5,691	\$ 2,854	\$ 1,311	\$ 9,856
Cost of Sales	3,092	2,793	254	6,139
Segment Net Income	2,001	6	937	2,944
Segment Assets	22,386	3,504	16,561	42,451
Expenditures for Segment Assets	\$ 5	\$ -	\$ -	\$ 5

NOTE 15 - RECENTLY ISSUED ACCOUNTING STANDARDS

In October 2009, the Financial Accounting Standards Board (FASB) issued amended revenue recognition guidance for arrangements with multiple deliverables. The new guidance eliminates the residual method of revenue recognition and allows the use of management's best estimate of selling price for individual elements of an arrangement when vendor specific objective evidence (VSOE), vendor objective evidence (VOE) or third-party evidence (TPE) is unavailable. For the Company, this guidance is effective for all new or materially modified arrangements entered into on or after October 1, 2011 with earlier application permitted as of the beginning of a fiscal year. Full retrospective application of the new guidance is optional. The Company is currently assessing its implementation of this new guidance, but does not expect a material impact on the consolidated financial statements.

In October 2009, the FASB issued guidance which amends the scope of existing software revenue recognition accounting. Tangible products containing software components and non-software components that function together to deliver the product's essential functionality would be scoped out of the accounting guidance on software and accounted for based on other appropriate revenue recognition guidance. For the Company, this guidance is effective for all new or materially modified arrangements entered into on or after October 1, 2011 with earlier application permitted as of the beginning of a fiscal year. Full retrospective application of the new guidance is optional. This guidance must be adopted in the same period that the Company adopts the amended accounting for arrangements with multiple deliverables described in the preceding paragraph. The Company is currently assessing its implementation of this new guidance, but does not expect a material impact on the consolidated financial statements.

On October 1, 2009, the Company adopted the revised FASB guidance regarding business combinations which was required to be applied to business combinations on a prospective basis. The revised guidance requires that the



acquisition method of accounting be applied to a broader set of business combinations, amends the definition of a business combination, provides a definition of a business, requires an acquirer to recognize an acquired business at its fair value at the acquisition date and requires the assets and liabilities assumed in a business combination to be measured and recognized at their fair values as of the acquisition date (with limited exceptions). There was no impact upon adoption and the effects of this guidance will depend on the nature and significance of business combinations occurring after the effective date.

In August 2009, the FASB issued guidance on the measurement of liabilities at fair value. The guidance provides clarification that in circumstances in which a quoted market price in an active market for an identical liability is not available, an entity is required to measure fair value using a valuation technique that uses the quoted price of an identical liability when traded as an asset or, if unavailable, quoted prices for similar liabilities or similar assets when traded as assets. If none of this information is available, an entity should use a valuation technique in accordance with existing fair valuation principles. The Company adopted this guidance in the quarter ended September 30, 2009 and there was no material impact on the consolidated financial statements.

On July 1, 2009, the FASB issued the FASB Accounting Standards Codification (the Codification). The Codification became the single source of authoritative nongovernmental U.S. GAAP, superseding existing FASB, American Institute of Certified Public Accountants (AICPA), Emerging Issues Task Force (EITF) and related literature. The Codification eliminates the previous US GAAP hierarchy and establishes one level of authoritative GAAP. All other literature is considered non-authoritative. The Codification was effective for interim and annual periods ending after September 15, 2009. The Company adopted the Codification for the year ending September 30, 2009. There was no impact to the consolidated financial results as this change is disclosure-only in nature.

In June 2009, the FASB issued amendments to the accounting rules for variable interest entities (VIEs) and for transfers of financial assets. The new guidance for VIEs eliminates the quantitative approach previously required for determining the primary beneficiary of a variable interest entity and requires ongoing qualitative reassessments of whether an enterprise is the primary beneficiary. In addition, qualifying special purpose entities (QSPEs) are no longer exempt from consolidation under the amended guidance. The amendments also limit the circumstances in which a financial asset, or a portion of a financial asset, should be derecognized when the transferor has not transferred the entire original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented, and/or when the transferor has continuing involvement with the transferred financial asset. The Company will adopt these amendments for interim and annual reporting periods beginning on October 1, 2010. The Company does not expect the adoption of these amendments to have a material impact on the consolidated financial statements.

In May 2009, the FASB issued guidelines on subsequent event accounting which sets forth: 1) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; 2) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements; and 3) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. These guidelines were effective for interim and annual periods ending after June 15, 2009, and the Company adopted them in the quarter ended June 30, 2009. There was no impact on the consolidated financial statements.

In April 2009, the FASB issued guidance on determining fair value when the volume and level of activity for an asset or liability has significantly decreased, and in identifying transactions that are not orderly. Based on the guidance, if an entity determines that the level of activity for an asset or liability has significantly decreased and that a transaction is not orderly, further analysis of transactions or quoted prices is needed, and a significant adjustment to the transaction or quoted prices may be necessary to estimate fair value. The guidance was effective on a prospective basis for interim and annual periods ending after June 15, 2009. The Company adopted this guidance in the quarter ended June 30, 2009, and there was no material impact on the consolidated financial statements.

In April 2009, the FASB issued guidance on the recognition and presentation of other-than-temporary impairments on investments in debt securities. If an entity's management asserts that it does not have the intent to sell a debt security and it is more likely than not that it will not have to sell the security before recovery of its cost basis, then an entity may separate other-than-temporary impairments into two components: 1) the amount related to credit losses (recorded in earnings), and 2) all other amounts (recorded in other comprehensive income). This guidance was effective on a prospective basis for interim and annual periods ending after June 15, 2009. The Company adopted this guidance for the quarter ended June 30, 2009, and there was no material impact on the consolidated financial statements.

In April 2009, the FASB issued additional requirements regarding interim disclosures about the fair value of financial instruments which were previously only disclosed on an annual basis. Entities are now required to disclose the fair value of financial instruments which are not recorded at fair value in the financial statements in both their interim and annual financial statements. The new requirements were effective for interim and annual periods ending after June 15, 2009 on a prospective basis. The Company adopted these requirements in the quarter ended June 30, 2009. There was no impact on the consolidated financial results as this relates only to additional disclosures.

In April 2009, the FASB issued an amendment to the revised business combination guidance regarding the accounting for assets acquired and liabilities assumed in a business combination that arise from contingencies. The requirements of this amended guidance carry forward without significant revision the guidance on contingencies which existed prior to January 1, 2009. Assets acquired and liabilities assumed in a business combination that arise from contingencies are recognized at fair value if fair value can be reasonably estimated. If fair value cannot be reasonably estimated, the asset or liability would generally be recognized in accordance with the Accounting Standards Codification (ASC) Topic 450 on contingencies. There was no impact upon adoption.

In April 2008, the FASB issued new requirements regarding the determination of the useful lives of intangible assets. In developing assumptions about renewal or extension options used to determine the useful life of an intangible asset, an entity needs to consider its own historical experience adjusted for entity-specific factors. In the absence of that experience, an entity shall consider the assumptions that market participants would use about renewal or extension options. The new requirements apply to intangible assets acquired after October 1, 2009. The adoption of these new rules did not have a material impact on the Consolidated Financial Statements.

In December 2007, the FASB issued new guidance on noncontrolling interests in consolidated financial statements. This guidance requires that the noncontrolling interest in the equity of a subsidiary be accounted for and reported as equity, provides revised guidance on the treatment of net income and losses attributable to the noncontrolling interest and changes in ownership interests in a subsidiary and requires additional disclosures that identify and distinguish between the interests of the controlling and noncontrolling owners. Pursuant to the transition provisions, the Company adopted this new guidance on October 1, 2009 via retrospective application of the presentation and disclosure requirements.

In March 2008, the FASB issued new disclosure requirements regarding derivative instruments and hedging activities. Entities must now provide enhanced disclosures on an interim and annual basis regarding how and why the entity uses derivatives; how derivatives and related hedged items are accounted for, and how derivatives and related hedged items affect the entity's financial position, financial results and cash flow. Pursuant to the transition provisions, the Company adopted these new requirements on October 1, 2009. These new requirements do not impact the consolidated financial results as they are disclosure-only in nature.

The FASB guidance on fair value measurements and disclosures became effective January 1, 2008. However, in February 2008, the FASB delayed the effective date regarding fair value measurements and disclosures of nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), to October 1, 2009. The adoption of these provisions related to nonfinancial assets and nonfinancial liabilities on October 1, 2009 did not have a material impact on the consolidated financial statements.

In June 2008, the FASB issued guidance in determining whether instruments granted in share-based payment transactions are participating securities. The guidance became effective on October 1, 2009 via retrospective application. According to the new guidance, unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and, therefore, are included in computing earnings per share (EPS) pursuant to the two-class method. The two-class method determines earnings per share for each class of common stock and participating securities according to dividends or dividend equivalents and their respective participation rights in undistributed earnings. The adoption of these provisions is not expected to have a material impact on the consolidated financial statements.

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

### SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

#### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is designed to provide information that is supplemental to, and should be read together with, the Company's consolidated financial statements and the accompanying notes contained in this quarterly report. Information in this Item 2 is intended to assist the reader in obtaining an understanding of the consolidated financial statements, the changes in certain key items in those financial statements from year to year, the primary factors that accounted for those changes, and any known trends or uncertainties that the Company is aware of that may have a material effect on the Company's future performance, as well as how certain accounting principles affect the consolidated financial statements. MD&A includes the following sections:

- Highlights and Executive Summary

- Results of Operations—an analysis of the Company’s consolidated results of operations, for the two years presented in the consolidated financial statements
- Liquidity and Capital Resources—an analysis of the effect of the Company’s operating, financing and investing activities on the Company’s liquidity and capital resources
- Off-Balance Sheet Arrangements—a discussion of such commitments and arrangements
- Critical Accounting Policies and Estimates—a discussion of accounting policies that require significant judgments and estimates
- New Accounting Pronouncements—a summary and discussion of the Company’s plans for the adoption of relevant new accounting standards

F-17

---

The following discussion contains forward-looking statements that reflect the Company's plans, estimates and beliefs. Actual results could differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those discussed below and elsewhere in this Prospectus particularly in "Special Note Regarding Forward-Looking Statements," "Market Data" and "Risk Factors."

### Highlights and Executive Summary

For the three months ended December 31, 2009, the Company reported revenues of \$12,714 thousand, an increase of 29% from revenues of \$9,856 thousand reported for the three months ended December 31, 2008. Net income was \$2,946 thousand for the three months ended December 31, 2009 as compared to \$2,944 thousand for the three months ended December 31, 2008. The Company continued to expand its video advertising membership base and generated a 49% increase in its trade services business segment as the Company's trade services business segment continued to recover from the 2008 global economic crisis. Net income for 2009 was also impacted by income taxes of \$883 thousand. The three months ended December 31, 2009 represented the first reporting period since 2006 where the Company's subsidiaries operating in China did not have a tax free holiday in effect. Taxes are being calculated using a blended rate based on assumptions associated with certain operations of the Company being taxed within mainland China and other operations being taxed outside of mainland China.

### Results of Operations

The following tables set forth key components of the Company's results of operations for the three months ended December 31, 2009 and December 31, 2008, respectively. All dollar amounts, except per share amounts referenced herein are "in thousands".

#### Three Months End December 31, 2009 and December 31, 2008

	December 31, 2009 (000's)	December 31, 2008 (000's)	Increase (Decrease )	Percentage Increase (Decrease )
Revenues	\$ 12,714	\$ 9,856	\$ 2,858	29%
Cost of Sales	7,111	6,139	972	16%
Gross Profit	5,603	3,717	1,886	51%
Operating Expenses	1,774	771	1,003	130%
Income From Operations	3,829	2,946	883	30%
Income Taxes	(883)	(2)	(881)	44,050%
Net Income	2,946	2,944	2	0%
Other Comprehensive Income	(81)	19	(100)	(5,000)%
Comprehensive Income	\$ 2,865	\$ 2,963	(98)	(3)%
<b>Earnings per Common Share</b>				
- Basic	\$ 0.47	\$ 1.53		
- Fully Diluted	\$ 0.47	\$ 1.53		
<b>Weighted Average Common Share Outstanding</b>				

- Basic	5,209,013	1,617,627
- Fully Diluted	5,231,013	1,617,627

Revenues increased by \$2,858 thousand:

Revenues totaled \$12,714 thousand for the three months ended December 31, 2009 compared to \$9,856 thousand for the three months ended December 31, 2008. The increase of \$2,858 thousand is due primarily to 21% and 49% growth in the online membership services and trading services business segments for the three months ended December 31, 2009 as compared to the three months ended December 31, 2008, respectively. During the three months ended December 31, 2009, Subaye will focus on further developing its online video advertising business. Our third Asian motion picture investment, Dayoucun, generated \$26 thousand in revenues for the period from release, December 22, 2009 through December 31, 2009. Dayoucun was released in theatres at the same time as certain other major motion pictures and faced very strong competition. We expect Dayoucun will produce more significant revenues in the next few months as the audiences in Asia begin to choose other motion pictures to view, in addition to the several extremely successful motion pictures currently playing in theatres.

Costs of Sales increased by \$972 thousand:

Costs of sales were \$7,111 thousand for the three months ended December 31, 2009 compared to \$6,139 thousand for the three months ended December 31, 2008. Costs of sales for the online membership services business segment decreased by 54% for the three months ended December 31, 2009 as compared to the three months ended December 31, 2008. The Company's www.subaye.com website was fully amortized as of September 30, 2009. As a result, costs of sales for the three months ended December 31, 2009 included amortization of the Company's secondary websites, SaaS software and related hardware and amortization of stock based compensation related to the two new merchant service provider contracts of \$189 thousand. . Also, cost of sales of the trading services segment increased by \$1,340 thousand due to increased sales and the entertainment media segment experienced a large increase in cost of sales, for advertising related to the release of a movie, in the amount of \$1,297 thousand.

Operating expenses increased by \$1,003 thousand:

For the three months ended December 31, 2009, we incurred operating expenses of \$1,774 thousand as compared to \$771 thousand for the three months ended December 31, 2008. Advertising expense was \$427 thousand and \$108 thousand for the three months ended December 31, 2009 and 2008, respectively. Stock-based compensation expense included in operating expenses totaled \$830 thousand and \$311 thousand for the three months ended December 31, 2009 and 2008, respectively. Certain significant stock based compensation was issued in the three months ended December 31, 2009 and in the fiscal year ended September 30, 2009. As a result, amortization of stock based compensation for the three months ended December 31, 2009 was significant. The full value of the stock issuances will be amortized over the term of the related contracts, many of which are for two or three years in length.

Net income increased by \$2 thousand:

Subaye generated net income of \$2,946 thousand for the three months ended December 31, 2009 as compared to \$2,944 thousand for the three months ended December 31, 2008. The Company was not subject to income taxes of any significant amount for the three months ended December 31, 2008 as a result of the PRC tax holidays granted to the Company for the years ended September 30, 2009 and 2008, respectively. During the three months ended December 31, 2009, the Company generated 29.9% net income growth when excluding the effect of income taxes for the three months ended December 31, 2009.

#### Liquidity and Capital Resources

As of December 31, 2009, we had a cash balance of \$2,668 thousand, consisting of money held in banks in mainland China and Hong Kong banks and cash in hand. We currently have no cash positions in the United States of America. We have been funding our operations through receipts from customers and equity-based financing such as the sale of our common stock, when needed.

Management has invested substantial time evaluating and considering numerous proposals for possible investments, acquisitions or business combinations, either sought out by management or presented to management by investment professionals, the Company's advisers and others. We continue to consider acquisitions, business combinations, or start up proposals, which could be advantageous to our shareholders. No assurance can be given that any such project, acquisition or combination will be concluded, or that all these actions will be approved by our Board of Directors.

Net cash provided by operations for the three months ended December 31, 2009 was \$314 thousand. We generated \$2,946 thousand in net income for the three months ended December 31, 2009. A total of \$1,347 thousand in depreciation and amortization was recorded for the three months ended December 31, 2009. We recorded \$1,040 thousand in amortization expense related to stock based compensation. Accounts receivable decreased by \$2,183



thousand. The net additional investments in copyrights for the three months ended December 31, 2009 totaled \$6,828 thousand.

Net cash provided by investing activities was \$0 for the three months ended December 31, 2009.

Net cash provided by financing activities for the three months ended December 31, 2009 was \$2,109 thousand. The Company raised \$2,109 thousand from bank loans with one year terms during the three months ended December 31, 2009.

Our future growth is dependent on our ability to execute on our business plans, raise capital for expansion, and to seek additional revenue sources. If we decide to pursue any acquisition opportunities or other expansion opportunities, we may need to raise additional capital, although there can be no assurances that such capital-raising activities would be successful.

#### Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements that will have a current or future effect on our financial condition and changes in financial condition in 2010 or 2009.

### Protection of Intellectual Property

The Company currently holds approximately \$24,386 thousand in copyrights covering programming rights for movies, internet broadcasts, DVDs and television programming. We cannot guarantee that if a competitor or anyone else were to commence litigation against us, we would be able to adequately defend our position and retain ownership and value in the intellectual property.

### Capital Requirements

In 2009 and 2008, the Company raised significant financing by issuing equity securities, namely the Company's common stock. If management determines that additional financing is necessary, we may not be able to continue to find adequate sources of financing in the future. Certain business segments in which we have committed to expanding operations, namely the "Entertainment Media" business segment, involve very significant capital requirements.

### Trends, Events, and Uncertainties

The present demand for our products will be dependent on, among other things, market acceptance of the Company's concept, the quality of its products, and general economic conditions which are cyclical in nature. The Company's business operations may be adversely affected by increased competition and prolonged recessionary periods in China.

### Critical Accounting Policies and Estimates

The discussion and analysis of our results of operations and liquidity and capital resources are based on our consolidated financial statements, which have been prepared in accordance with GAAP. In connection with the preparation of consolidated financial statements, the Company is required to make assumptions and estimates about future events, and apply judgments that affect the reported amounts of assets, liabilities, revenue, expenses, and the related disclosures. The assumptions, estimates and judgments included within these estimates are based on historical experience, current trends and other factors we believe to be relevant at the time the consolidated financial statements were prepared. On a regular basis, the accounting policies, assumptions, estimates and judgments are reviewed to ensure that the consolidated financial statements are presented fairly and in accordance with GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ from the assumptions and estimates, and such differences could be material.

The preparation of consolidated financial statements in conformity with GAAP requires us to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosures of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Significant estimates and assumptions are used for, but are not limited to: (1) asset impairments and (2) depreciable lives of assets. Future events and their effects cannot be predicted with certainty, and accordingly, accounting estimates require the exercise of judgment. The accounting estimates used in the preparation of the consolidated financial statements will change as new events occur, as more experience is acquired, as additional information is obtained and as our operating environment changes. We evaluate and update these assumptions and estimates on an ongoing basis and may employ outside experts to assist with these evaluations. Actual results could differ from the estimates that have been used.

Significant accounting policies are discussed in Note 1, Summary of Significant Accounting Policies, to the accompanying consolidated financial statements. We believe the following accounting policies are the most critical to aid in fully understanding and evaluating our reported financial results, as they require management to make difficult, subjective or complex judgments, and to make estimates about the effect of matters that are inherently uncertain.

Description	Judgments and Uncertainties	Effect if Actual Results Differ from Assumptions
-------------	-----------------------------	--

Impairment of Long Lived Assets

The carrying amounts of long-lived assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts.

These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to recoverable amount. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate selling price because quoted market prices for the Company's assets or cash-generating units are not readily available. In determining the value in use, expected cash flows generated by the asset or the cash-generating unit are discounted to their present value, which requires significant judgment relating to level of sales volume, selling price and amount of operating costs. The Company uses all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of sales volume, selling price and amount of operating costs.

Estimates contemplated by the Company with regard to the recoverability of carrying amounts for its long lived assets may prove to be inaccurate, in which case property, plant and equipment may be understated or overstated. In the future, if property, plant and equipment are determined to be overvalued, the Company would be required to recognize such costs in operating expenses at the time of such determination. Likewise, if property, plant and equipment are determined to be undervalued, operating expenses may have been over-reported in previous periods and the Company would be required to recognize such additional operating income at the time of sale.

## New Accounting Policies and Pronouncements

In October 2009, the Financial Accounting Standards Board (FASB) issued amended revenue recognition guidance for arrangements with multiple deliverables. The new guidance eliminates the residual method of revenue recognition and allows the use of management's best estimate of selling price for individual elements of an arrangement when vendor specific objective evidence (VSOE), vendor objective evidence (VOE) or third-party evidence (TPE) is unavailable. For the Company, this guidance is effective for all new or materially modified arrangements entered into on or after October 1, 2011 with earlier application permitted as of the beginning of a fiscal year. Full retrospective application of the new guidance is optional. The Company is currently assessing its implementation of this new guidance, but does not expect a material impact on the consolidated financial statements.

In October 2009, the FASB issued guidance which amends the scope of existing software revenue recognition accounting. Tangible products containing software components and non-software components that function together to deliver the product's essential functionality would be scoped out of the accounting guidance on software and accounted for based on other appropriate revenue recognition guidance. For the Company, this guidance is effective for all new or materially modified arrangements entered into on or after October 1, 2011 with earlier application permitted as of the beginning of a fiscal year. Full retrospective application of the new guidance is optional. This guidance must be adopted in the same period that the Company adopts the amended accounting for arrangements with multiple deliverables described in the preceding paragraph. The Company is currently assessing its implementation of this new guidance, but does not expect a material impact on the consolidated financial statements.

On October 1, 2009, the Company adopted the revised FASB guidance regarding business combinations which was required to be applied to business combinations on a prospective basis. The revised guidance requires that the acquisition method of accounting be applied to a broader set of business combinations, amends the definition of a business combination, provides a definition of a business, requires an acquirer to recognize an acquired business at its fair value at the acquisition date and requires the assets and liabilities assumed in a business combination to be measured and recognized at their fair values as of the acquisition date (with limited exceptions). There was no impact upon adoption and the effects of this guidance will depend on the nature and significance of business combinations occurring after the effective date.

In August 2009, the FASB issued guidance on the measurement of liabilities at fair value. The guidance provides clarification that in circumstances in which a quoted market price in an active market for an identical liability is not available, an entity is required to measure fair value using a valuation technique that uses the quoted price of an identical liability when traded as an asset or, if unavailable, quoted prices for similar liabilities or similar assets when traded as assets. If none of this information is available, an entity should use a valuation technique in accordance with existing fair valuation principles. The Company adopted this guidance in the quarter ended September 30, 2009 and there was no material impact on the consolidated financial statements.

On July 1, 2009, the FASB issued the FASB Accounting Standards Codification (the Codification). The Codification became the single source of authoritative nongovernmental U.S. GAAP, superseding existing FASB, American Institute of Certified Public Accountants (AICPA), Emerging Issues Task Force (EITF) and related literature. The Codification eliminates the previous US GAAP hierarchy and establishes one level of authoritative GAAP. All other literature is considered non-authoritative. The Codification was effective for interim and annual periods ending after September 15, 2009. The Company adopted the Codification for the year ending September 30, 2009. There was no impact to the consolidated financial results as this change is disclosure-only in nature.

In June 2009, the FASB issued amendments to the accounting rules for variable interest entities (VIEs) and for transfers of financial assets. The new guidance for VIEs eliminates the quantitative approach previously required for determining the primary beneficiary of a variable interest entity and requires ongoing qualitative reassessments of

whether an enterprise is the primary beneficiary. In addition, qualifying special purpose entities (QSPEs) are no longer exempt from consolidation under the amended guidance. The amendments also limit the circumstances in which a financial asset, or a portion of a financial asset, should be derecognized when the transferor has not transferred the entire original financial asset to an entity that is not consolidated with the transferor in the financial statements being presented, and/or when the transferor has continuing involvement with the transferred financial asset. The Company will adopt these amendments for interim and annual reporting periods beginning on October 1, 2010. The Company does not expect the adoption of these amendments to have a material impact on the consolidated financial statements.

In May 2009, the FASB issued guidelines on subsequent event accounting which sets forth: 1) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; 2) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements; and 3) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. These guidelines were effective for interim and annual periods ending after June 15, 2009, and the Company adopted them in the quarter ended June 30, 2009. There was no impact on the consolidated financial statements.

In April 2009, the FASB issued guidance on determining fair value when the volume and level of activity for an asset or liability has significantly decreased, and in identifying transactions that are not orderly. Based on the guidance, if an entity determines that the level of activity for an asset or liability has significantly decreased and that a transaction is not orderly, further analysis of transactions or quoted prices is needed, and a significant adjustment to the transaction or quoted prices may be necessary to estimate fair value. The guidance was effective on a prospective basis for interim and annual periods ending after June 15, 2009. The Company adopted this guidance in the quarter ended June 30, 2009, and there was no material impact on the consolidated financial statements.

In April 2009, the FASB issued guidance on the recognition and presentation of other-than-temporary impairments on investments in debt securities. If an entity's management asserts that it does not have the intent to sell a debt security and it is more likely than not that it will not have to sell the security before recovery of its cost basis, then an entity may separate other-than-temporary impairments into two components: 1) the amount related to credit losses (recorded in earnings), and 2) all other amounts (recorded in other comprehensive income). This guidance was effective on a prospective basis for interim and annual periods ending after June 15, 2009. The Company adopted this guidance for the quarter ended June 30, 2009, and there was no material impact on the consolidated financial statements.

In April 2009, the FASB issued additional requirements regarding interim disclosures about the fair value of financial instruments which were previously only disclosed on an annual basis. Entities are now required to disclose the fair value of financial instruments which are not recorded at fair value in the financial statements in both their interim and annual financial statements. The new requirements were effective for interim and annual periods ending after June 15, 2009 on a prospective basis. The Company adopted these requirements in the quarter ended June 30, 2009. There was no impact on the consolidated financial results as this relates only to additional disclosures.

In April 2009, the FASB issued an amendment to the revised business combination guidance regarding the accounting for assets acquired and liabilities assumed in a business combination that arise from contingencies. The requirements of this amended guidance carry forward without significant revision the guidance on contingencies which existed prior to January 1, 2009. Assets acquired and liabilities assumed in a business combination that arise from contingencies are recognized at fair value if fair value can be reasonably estimated. If fair value cannot be reasonably estimated, the asset or liability would generally be recognized in accordance with the Accounting Standards Codification (ASC) Topic 450 on contingencies. There was no impact upon adoption.

In April 2008, the FASB issued new requirements regarding the determination of the useful lives of intangible assets. In developing assumptions about renewal or extension options used to determine the useful life of an intangible asset, an entity needs to consider its own historical experience adjusted for entity-specific factors. In the absence of that experience, an entity shall consider the assumptions that market participants would use about renewal or extension options. The new requirements apply to intangible assets acquired after October 1, 2009. The adoption of these new rules did not have a material impact on the Consolidated Financial Statements.

In December 2007, the FASB issued new guidance on noncontrolling interests in consolidated financial statements. This guidance requires that the noncontrolling interest in the equity of a subsidiary be accounted for and reported as equity, provides revised guidance on the treatment of net income and losses attributable to the noncontrolling interest

and changes in ownership interests in a subsidiary and requires additional disclosures that identify and distinguish between the interests of the controlling and noncontrolling owners. Pursuant to the transition provisions, the Company adopted this new guidance on October 1, 2009 via retrospective application of the presentation and disclosure requirements.

In March 2008, the FASB issued new disclosure requirements regarding derivative instruments and hedging activities. Entities must now provide enhanced disclosures on an interim and annual basis regarding how and why the entity uses derivatives; how derivatives and related hedged items are accounted for, and how derivatives and related hedged items affect the entity's financial position, financial results and cash flow. Pursuant to the transition provisions, the company adopted these new requirements on October 1, 2009. These new requirements do not impact the consolidated financial results as they are disclosure-only in nature.

The FASB guidance on fair value measurements and disclosures became effective January 1, 2008. However, in February 2008, the FASB delayed the effective date regarding fair value measurements and disclosures of nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), to October 1, 2009. The adoption of these provisions related to nonfinancial assets and nonfinancial liabilities on October 1, 2009 did not have a material impact on the consolidated financial statements.

In June 2008, the FASB issued guidance in determining whether instruments granted in share-based payment transactions are participating securities. The guidance became effective on October 1, 2009 via retrospective application. According to the new guidance, unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents are participating securities and, therefore, are included in computing earnings per share (EPS) pursuant to the two-class method. The two-class method determines earnings per share for each class of common stock and participating securities according to dividends or dividend equivalents and their respective participation rights in undistributed earnings. The adoption of these provisions is not expected to have a material impact on the consolidated financial statements.



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

Not required for smaller reporting companies.

### ITEM 4T. CONTROLS AND PROCEDURES

#### Evaluation of Disclosure Controls and Procedures

Our management is responsible for establishing and maintaining a system of disclosure controls and procedures (as defined in Rule 13a-15(e)) under the Exchange Act) that is designed to ensure that information required to be disclosed by the Company in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Pursuant to Rule 13a-15(b) under the Exchange Act, the Company carried out an evaluation with the participation of the Company's management, the Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), of the effectiveness of the Company's disclosure controls and procedures (as defined under Rule 13a-15(e) under the Exchange Act) as of the three months ended December 31, 2009. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that as of December 31, 2009, our disclosure controls and procedures were not effective at the reasonable assurance level due to the material weaknesses described below.

In light of the material weaknesses described below, we performed additional analysis and other post-closing procedures to ensure our financial statements were prepared in accordance with generally accepted accounting principles. Accordingly, we believe that the financial statements included in this report fairly present, in all material respects, our financial condition, results of operations and cash flows for the periods presented.

A material weakness is a control deficiency (within the meaning of the Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 5) or combination of control deficiencies, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected. Management has identified the following three material weaknesses which have caused management to conclude that, as of December 31, 2009, our disclosure controls and procedures were not effective at the reasonable assurance level:

1. Management's conclusion is based on, among other things, the audit adjustments recorded for fiscal years 2009 and 2008, and for the lack of segregation of duties and responsibilities within the Organization.

It should be noted that any system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system are met. In addition, the design of any control system is based in part upon certain assumptions about the likelihood of future events. Because of these and other inherent limitations of control systems, there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

#### Remediation of Material Weaknesses

To remediate the material weaknesses in our disclosure controls and procedures identified above, we are developing a plan to ensure that all information will be recorded, processed, summarized and reported accurately, and as of the date

of this report, we have taken the following steps to address the above-referenced material weaknesses in our internal control over financial reporting:

1. We will continue to educate our management personnel to comply with the disclosure requirements of Securities Exchange Act of 1934 and Regulation S-K; and

2. We will increase management oversight of accounting and reporting functions in the future.

#### CHANGES IN INTERNAL CONTROL OVER FINANCIAL

No changes in the Company's internal control over financial reporting have come to management's attention during the Company's last fiscal quarter that have materially affected, or are likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

We may be involved in litigation, negotiation and settlement matters that may occur in our day-to-day operations. Management does not believe the implication of this type of litigation will have a material impact on our consolidated financial statements.

ITEM 1A. RISK FACTORS

Not required for smaller reporting companies.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS

(a)	Exhibits
31.1	Rule 13a-14(a)/15d-14(a) Certification (CEO)
31.2	Rule 13a-14(a)/15d-14(a) Certification (CFO)
32.1	Section 1350 Certification (CEO)
32.2	Section 1350 Certification (CFO)

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SUBAYE, INC.

Date: February 16, 2010

By:

/s/ Zhiguang Cai  
Zhiguang Cai  
Chief Executive Officer and President  
(Principal Executive Officer)

Date: February 16, 2010

By:

/s/ James T. Crane  
James T. Crane  
Chief Financial Officer  
(Principal Financial and Accounting  
Officer)