

SINA CORP  
Form 10-Q  
August 09, 2006

**Table of Contents**

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

**FORM 10-Q**

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

**For the quarterly period ended June 30, 2006**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number 000-30698**

**SINA CORPORATION  
(Exact Name of Registrant as Specified in Its Charter)**

**Cayman Islands  
(State or other jurisdiction of  
incorporation or organization)**

**52-2236363  
(I.R.S. Employer  
Identification Number)**

**Room 1802, United Plaza  
1468 Nan Jing Road West  
Shanghai 200040, China  
(86-21) 6289 5678**

**(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)**

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 (the Exchange Act) during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

The number of the registrant's ordinary shares outstanding as of August 4, 2006 was 53,609,908.

**SINA CORPORATION  
INDEX**

	<b>Page no.</b>
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
<u>Item 1. Condensed Consolidated Financial Statements:</u>	3
<u>Condensed Consolidated Balance Sheets at June 30, 2006 and December 31, 2005</u>	3
<u>Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2006 and 2005</u>	4
<u>Condensed Consolidated Statements of Shareholders' Equity and Comprehensive Income for the six months ended June 30, 2006 and 2005</u>	5
<u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2006 and 2005</u>	6
<u>Notes to Condensed Consolidated Financial Statements</u>	7
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	15
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	24
<u>Item 4. Controls and Procedures</u>	25
<b><u>PART II. OTHER INFORMATION</u></b>	25
<u>Item 1. Legal Proceedings</u>	25
<u>Item 1A. Risk Factors</u>	26
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	42
<u>Item 3. Defaults Upon Senior Securities</u>	42
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	42
<u>Item 5. Other Information</u>	42
<u>Item 6. Exhibits</u>	43
<u>Signature</u>	44
<u>EXHIBIT 31.1</u>	
<u>EXHIBIT 31.2</u>	
<u>EXHIBIT 32.1</u>	
<u>EXHIBIT 32.2</u>	

**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Condensed Consolidated Financial Statements**

**SINA CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(Unaudited, in thousands, except per share data)

	<b>June 30, 2006</b>	<b>December 31, 2005</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 116,716	\$ 88,410
Short-term investments	195,765	212,279
Accounts receivable, net of allowances for doubtful accounts of \$3,453 and \$2,443, respectively	44,895	33,940
Short-term deferred tax assets	865	857
Prepaid expenses and other current assets	8,690	11,523
<b>Total current assets</b>	<b>366,931</b>	<b>347,009</b>
Investment in Tidetime Sun	740	716
Property and equipment, net	23,248	22,207
Equity investments	2,247	3,261
Intangible assets, net	8,754	9,691
Goodwill	82,663	82,663
Other assets	2,619	3,174
<b>Total assets</b>	<b>\$ 487,202</b>	<b>\$ 468,721</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 1,120	\$ 1,582
Accrued liabilities	36,834	43,235
Income taxes payable	4,855	4,282
<b>Total current liabilities</b>	<b>42,809</b>	<b>49,099</b>
Convertible debt	100,000	100,000
<b>Total liabilities</b>	<b>142,809</b>	<b>149,099</b>
Commitments and contingencies (Note 13)		
Shareholders equity:		
Ordinary shares: \$0.133 par value; 150,000 shares authorized; 53,605 and 53,265 shares issued and outstanding	7,129	7,084
Additional paid-in capital	290,991	284,559
Retained earnings	43,532	26,057
Accumulated other comprehensive income (loss):		

Edgar Filing: SINA CORP - Form 10-Q

Unrealized loss on investments in marketable securities	(4,224)	(2,903)
Cumulative translation adjustments	6,965	4,825
Total shareholders' equity	344,393	319,622
Total liabilities and shareholders' equity	\$ 487,202	\$ 468,721

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

3

---

**Table of Contents**

**SINA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(Unaudited, in thousands, except per share data)**

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net revenues:				
Advertising	\$ 29,454	\$ 20,373	\$ 51,635	\$ 37,021
Non-advertising	24,224	25,757	48,755	54,957
	53,678	46,130	100,390	91,978
Cost of revenues:				
Advertising (*)	10,317	6,541	18,615	12,435
Non-advertising	9,343	7,794	19,090	16,834
	19,660	14,335	37,705	29,269
Gross profit	34,018	31,795	62,685	62,709
Operating expenses:				
Sales and marketing (*)	13,497	10,718	25,302	22,202
Product development (*)	4,993	3,520	9,603	7,222
General and administrative (*)	7,427	5,078	12,584	9,775
Amortization of intangible assets	469	1,041	937	2,082
	26,386	20,357	48,426	41,281
Income from operations	7,632	11,438	14,259	21,428
Interest and other income	2,012	1,564	3,952	3,096
Amortization of convertible debt issuance cost	(171)	(171)	(342)	(342)
Gain (loss) on sales of investments and investment in Tidetime Sun	2,006	(1,338)	1,794	(1,282)
Loss on equity investments	(162)	(858)	(505)	(1,424)
Income before income taxes	11,317	10,635	19,158	21,476
Provision for income taxes	(878)	(682)	(1,683)	(1,213)
Net income	\$ 10,439	\$ 9,953	\$ 17,475	\$ 20,263
Basic net income per share	\$ 0.19	\$ 0.19	\$ 0.33	\$ 0.39
Shares used in computing basic income per share	53,554	52,111	53,496	51,771
Diluted net income per share	\$ 0.18	\$ 0.17	\$ 0.30	\$ 0.35
Shares used in computing diluted income per share	58,444	58,783	58,522	58,642

(\*) Cost of revenues and operating expenses for the three and six months ended June 30, 2006 included stock-based compensation expense in accordance with SFAS 123R, which the Company adopted on January 1, 2006. See Note 10 Stock-Based Compensation to the Condensed Consolidated Financial Statements for additional information.

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

**Table of Contents**

**SINA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY**  
**AND COMPREHENSIVE INCOME**  
(Unaudited, in thousands)

	<b>Ordinary Shares</b>		<b>Additional</b>	<b>Retained</b>	<b>Accumulated</b>	<b>Total</b>
	<b>Shares</b>	<b>Amount</b>	<b>Paid-in</b>	<b>Earnings</b>	<b>Other</b>	<b>Shareholders</b>
			<b>Capital</b>		<b>Income(Loss)</b>	<b>Equity</b>
Balances at December 31, 2005	53,265	\$ 7,084	\$ 284,559	\$ 26,057	\$ 1,922	\$ 319,622
Comprehensive income:						
Net income				17,475		17,475
Unrealized loss on marketable securities					(1,321)	(1,321)
Currency translation adjustments					2,140	2,140
Total comprehensive income						18,294
Stock-based compensation			4,539			4,539
Issuance of ordinary shares pursuant to stock plans	156	20	1,918			1,938
Business acquisition	184	25	(25)			
Balances at June 30, 2006	53,605	\$ 7,129	\$ 290,991	\$ 43,532	\$ 2,741	\$ 344,393
				<b>Retained</b>	<b>Accumulated</b>	<b>Total</b>
	<b>Ordinary Shares</b>	<b>Amount</b>	<b>Additional</b>	<b>Earnings</b>	<b>Other</b>	<b>Shareholders</b>
	<b>Shares</b>		<b>Paid-in</b>	<b>(Accumulated</b>	<b>Comprehensive</b>	<b>Equity</b>
			<b>Capital</b>	<b>Deficit)</b>	<b>Income(Loss)</b>	
Balances at December 31, 2004	51,359	\$ 6,834	\$ 263,912	\$ (17,058)	\$ (343)	\$ 253,345
Comprehensive income:						
Net income				20,263		20,263
Unrealized loss on marketable securities					(1,380)	(1,380)
Currency translation adjustments					10	10
Total comprehensive income						18,893
Issuance of ordinary shares pursuant to stock	1,436	191	4,774			4,965



plans							
Business acquisition	275	37	11,198				11,235
Balances at June 30, 2005	53,070	\$ 7,062	\$ 279,884	\$ 3,205	\$ (1,713)	\$	288,438

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

**Table of Contents**

**SINA CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(Unaudited, in thousands)**

	<b>Six months ended</b>	
	<b>June 30,</b>	
	<b>2006</b>	<b>2005</b>
Cash flows from operating activities:		
Net income	\$ 17,475	\$ 20,263
Adjustments to reconcile net income to net cash provided by operating activities:		
Changes in allowance for doubtful accounts	1,891	1,097
(Gain) loss on sales of investments and investments in Tidetime Sun	(1,794)	1,282
Loss on equity investments	505	1,424
Depreciation	4,673	4,372
Stock-based compensation	4,539	
Amortization of convertible debt issuance cost	342	342
Amortization of intangible assets	937	2,082
Changes in assets and liabilities:		
Accounts receivable	(12,507)	6,423
Prepaid expenses and other current assets	(261)	2,644
Accounts payable	(473)	31
Accrued liabilities	4,490	(6,741)
Income taxes payable	531	(960)
Other assets	223	(1,421)
Net cash provided by operating activities	20,571	30,838
Cash flows from investing activities:		
Proceeds from sale of short-term investments	16,460	1,206
Cash paid for business acquisition	(11,266)	(16,891)
Purchases of property and equipment	(5,515)	(7,792)
Cash paid for equity investments		(2,819)
Proceeds from sale of investments	5,578	286
Net cash provided by (used in) investing activities	5,257	(26,010)
Cash flows from financing activities:		
Proceeds from issuance of ordinary shares	1,938	4,965
Net cash provided by financing activities	1,938	4,965
Effect of exchange rate change on cash and cash equivalents	540	
Net increase in cash and cash equivalents	28,306	9,793
Cash and cash equivalents at the beginning of the period	88,410	153,768
Cash and cash equivalents at the end of the period	\$ 116,716	\$ 163,561

Supplemental disclosure of significant noncash activities:

Ordinary shares issued for business acquisition	\$ 4,145	\$ 11,235
---	----------	-----------

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

6

---

**Table of Contents**

**SINA CORPORATION**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**1. Business**

SINA Corporation ( SINA or the Company ), a Cayman Islands corporation, is a leading online media company and value-added information service provider in the People's Republic of China (the PRC or China ) and the global Chinese communities. With a branded network of localized websites targeting Greater China and overseas Chinese, the Company provides services through five major business lines including SINA.com (online news and content), SINA Mobile (mobile value-added services or MVAS ), SINA Online (community-based services and games), SINA.net (search and enterprise services) and SINA E-Commerce (online shopping). Together these business lines provide an array of services including region-focused online portals, MVAS, search and directory, interest-based and community-building channels, free and premium email, audio and video streaming, online games, virtual ISP, classified listings, fee-based services, e-commerce and enterprise e-solutions.

**2. Summary of Significant Accounting Policies*****Principles of consolidation and basis of presentation***

The accompanying interim condensed consolidated financial statements have been prepared in conformity with the generally accepted accounting principles in the United States of America ( GAAP ), consistent in all material respects with those applied in the Company's Annual Report on Form 10-K for the year ended December 31, 2005. The interim financial information is unaudited but reflects all adjustments which are, in the opinion of management, necessary to provide fair condensed consolidated balance sheets, condensed consolidated statements of operations, condensed consolidated statements of shareholders' equity and comprehensive income and condensed consolidated statements of cash flows for the interim periods presented. Such adjustments are normal and recurring except as otherwise noted. The Condensed Consolidated Balance Sheets as of December 31, 2005 are derived from the December 31, 2005 audited financial statements, but do not include all disclosures required by accounting principles generally accepted in the United States of America. You should read these interim condensed consolidated financial statements in conjunction with the audited financial statements, including the notes thereto, and the other information set forth in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

The condensed consolidated financial statements include the accounts of the Company, its subsidiaries and variable interest entities ( VIEs ) for which the Company is the primary beneficiary. All significant intercompany accounts and transactions have been eliminated. Investments in entities in which the Company can exercise significant influence, but which are less than majority owned and not otherwise controlled by the Company, are accounted for under the equity method. The Company has adopted Financial Accounting Standards Board ( FASB ) Interpretation No. ( FIN ) 46R Consolidation of Variable Interest Entities ( FIN 46R ), an Interpretation of Accounting Research Bulletin No. 51,

Consolidated Financial Statements. FIN 46R requires a VIE to be consolidated by a company if that company is subject to a majority of the risk of loss for the VIEs or is entitled to receive a majority of the VIE's residual returns. To comply with PRC laws and regulations, the Company provides substantially all its Internet content provision, MVAS and advertising services in China via its VIEs. These VIEs are wholly or partially owned by certain employees of the Company. The capital for the VIEs are funded by the Company and recorded as interest-free loans to these PRC employees. These loans were eliminated with the capital of the VIEs during consolidation. As of June 30, 2006, the total amount of interest-free loans to these PRC employees was \$9.6 million. The aggregate accumulated losses of all VIEs as of June 30, 2006 were approximately \$5.7 million and have been included in the condensed consolidated financial statements.

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and such differences may be material to the financial statements. Certain prior year amounts have been reclassified to conform to the current year presentation.

***Stock-based compensation***

Edgar Filing: SINA CORP - Form 10-Q

Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement No. 123 (revised 2004), Share-Based Payment ( SFAS 123R ), which revises FASB Statement No. 123, Accounting-Based Compensation ( SFAS 123 ) and supersedes Accounting Principles Board ( APB ) Opinion No. 25, Accounting for Stock Issued to Employees ( APB 25 ). Under the fair value recognition provisions of SFAS 123R, the Company is required to measure the cost of employee services

**Table of Contents**

received in exchange for stock-based compensation measured at the grant date fair value of the award. The Company recognizes the compensation costs, net of a forfeiture rate, on a straight-line basis over the requisite service period of the award, which is generally the option vesting term of four years. In March 2005, the Securities & Exchange Commission issued Staff Accounting Bulletin No. 107 ( SAB 107 ) relating to SFAS 123R. The Company has applied the provisions of SAB 107 in its adoption of SFAS 123R.

The Company elected the modified prospective method and therefore has not restated results for prior periods. The valuation provisions of SFAS 123R apply to new grants and grants that were outstanding as of the effective date. Estimated compensation for grants that were outstanding as of the effective date are recognized over the remaining service period using the compensation cost estimated for the SFAS 123 pro forma disclosures.

In conjunction with the adoption of SFAS 123R, the Company changed its method of attributing the value of stock compensation expense from accelerated basis to straight-line basis. Compensation expense for share-based payment awards granted prior to fiscal 2006 will continue to be recognized using the accelerated basis while compensation expense for awards granted after the effective date are recognized using the straight-line basis.

SFAS 123R requires forfeitures to be estimated at the time of grant and revised in subsequent periods if actual forfeitures differ from those estimates. Compensation cost estimated for the SFAS 123 pro forma disclosures accounted for forfeitures as they occur. See Note 10 for further discussion on stock-based compensation.

***Recent accounting pronouncements***

In July 2006, the Financial Accounting Standards Board ( FASB ) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 ( FIN 48 ), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in its financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective for the Company on January 1, 2007, with the cumulative effect of the change in accounting principle, if any, recorded as an adjustment to opening retained earnings. The Company is currently evaluating the impact of adopting FIN 48 on its consolidated financial position, cash flows and results of operations.

**3. Short-Term Investments**

The investments in marketable debt securities are classified as available-for-sale securities. The Company invests in these securities with the intent to make such funds readily available for operating or acquisition purposes and, accordingly, classifies them as short-term investments. The following table summarizes the contractual maturities of available-for-sale debt securities:

	<b>June 30, 2006</b>	<b>December 31, 2005</b>
	<b>(in thousands)</b>	
Short-term investments:		
Due within one year	\$ 164,595	\$ 173,657
Due one to five years	18,529	24,688
Due after five years	12,641	13,934
	<b>\$ 195,765</b>	<b>\$ 212,279</b>

During the three and six months ended June 30, 2006, the Company recorded unrealized losses of \$1.0 million and \$1.3 million, respectively, and recorded an unrealized gain of \$0.5 million and \$0.1 million, in the same periods of 2005, respectively, on its marketable debt securities as a component of comprehensive income. The Company considered the declines in value as not other-than-temporary, because the declines in market value were attributable to changes in interest rates, not credit quality, and because the Company has the ability and intent to hold these investments until a recovery of fair value, which may be maturity.

**4. Investment in Tidetime Sun**

Investment in Tidetime Sun is accounted for as an investment in marketable equity securities under the provisions of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, and is classified as available for sale. The fair value of this investment as of June 30, 2006 was \$0.7 million, compared to a cost basis of \$0.7 million. If there is a decline in fair value that is deemed to be other-than-temporary, the Company may have to recognize impairment charges in future periods.

**Table of Contents****5. Equity Investments**

Equity investments are comprised of investments in privately held companies and are accounted for using the equity method of accounting. In May 2006, the Company sold its interest in Shanghai-NC SINA, a joint venture with NC Soft, a Korean online game company, to NC Soft. The Company recorded a gain of \$2.0 million from this transaction.

The following sets forth the changes in the Company's equity investments:

	<b>Shanghai NC-SINA</b>	<b>COAL *</b>	<b>Others</b>	<b>Total</b>
	<b>(in thousands)</b>			
Balances at December 31, 2005	\$ 1,417	\$	\$1,844	\$ 3,261
Additional investment			800	800
Share of loss on equity investments	(108)		(397)	(505)
Sale of investment	(1,309)			(1,309)
Balances at June 30, 2006	\$	\$	\$2,247	\$ 2,247

  

	<b>Shanghai NC-SINA</b>	<b>COAL</b>	<b>Others</b>	<b>Total</b>
	<b>(in thousands)</b>			
Balances at December 31, 2004	\$ 1,384	\$ 1,932	\$ 1,225	\$ 4,541
Additional investment		1,749	1,070	2,819
Share of gain (loss) on equity investments	257	(1,498)	(183)	(1,424)
Balances at June 30, 2005	\$ 1,641	\$ 2,183	\$ 2,112	\$ 5,936

\* Equity investment in China Online Auction Limited (COAL, a.k.a. 1Pai.com), a joint venture with Yahoo! Inc., was sold to Alibaba.com in December 2005.

**6. Intangible Assets**

The following table summarizes intangible assets, net:

	<b>June 30, 2006</b>		<b>December 31, 2005</b>			
	<b>Cost</b>	<b>Accumulated amortization</b>	<b>Net</b>	<b>Cost</b>	<b>Accumulated amortization</b>	<b>Net</b>
	<b>(in thousands)</b>					
Non-compete agreements	3,627	(3,113)	514	3,627	(2,691)	936
Technology	10,300	(2,060)	8,240	10,300	(1,545)	8,755



Edgar Filing: SINA CORP - Form 10-Q

\$ 13,927      \$ (5,173)      \$ 8,754      \$ 13,927      \$ (4,236)      \$ 9,691

The intangible assets are all amortizable. Non-compete agreements have original estimated useful lives of eighteen to thirty-six months. Technology has original estimated useful life of ten years.

Amortization expense related to intangible assets were \$0.5 million and \$0.9 million for the three and six months ended June 30, 2006, respectively, and \$1.0 million and \$2.1 million for the three and six months ended June 30, 2005, respectively. As of June 30, 2006, estimated amortization expenses in future periods are expected to be as follows:

<b>Fiscal year</b>	<b>Amortization expenses (in thousands)</b>
Remainder of 2006	\$ 883
2007	1,176
2008	1,030
2009	1,030
2010	1,030
Thereafter	3,605
Total expected amortization expense	\$ 8,754

**7. Accrued Liabilities**

During the three months ended March 31, 2006, the Company paid \$11.3 million in cash to the prior shareholders of Crillion

**Table of Contents**

Corporation for the achievement of the 2005 performance target which was accrued as of December 31, 2005.

**8. Income Taxes**

The Company is registered in the Cayman Islands and has operations in four tax jurisdictions, including China, the United States, Hong Kong and Taiwan. The operations in Taiwan represent a branch office of the subsidiary in the United States. For operations in the United States, Hong Kong and Taiwan, the Company has incurred net accumulated operating losses for income tax purposes. The Company believes that it is more likely than not that these net accumulated operating losses will not be utilized in the future. Therefore, the Company has provided full valuation allowance for the deferred tax assets arising from the losses at these locations as of June 30, 2006. The Company generated substantially all of its net income from its China operations for the three and six months ended June 30, 2006 and 2005, and the Company has recorded income tax provisions for the periods as follows:

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
	<b>(in thousands, except percentages)</b>		<b>(in thousands, except percentages)</b>	
Loss subject to non China operation	\$ (1,944)	\$ (3,716)	\$ (4,859)	\$ (6,101)
Income subject to China operation	13,261	14,351	24,017	27,577
Income before taxes	\$ 11,317	\$ 10,635	\$ 19,158	\$ 21,476
Income tax expenses subject to China operation	\$ 878	\$ 682	\$ 1,683	\$ 1,213
Effective tax rate for China operation	7%	5%	7%	4%

Pursuant to PRC Income Tax Laws, the Company's subsidiaries and VIEs are generally subject to Enterprise Income Taxes ( EIT ) at a statutory rate of 33%, which comprises 30% national income tax and 3% local income tax. Some of these subsidiaries and VIEs are qualified new technology enterprises and under PRC Income Tax Laws, they are subject to the preferential tax rate of 15%. In addition, some of the Company's subsidiaries are Foreign Investment Enterprise and under PRC Income Tax Laws, they are entitled to either a three-year tax exemption followed by three years with a 50% reduction in the tax rate, commencing the first operating year, or a two-year tax exemption followed by three years with a 50% reduction in the tax rate, commencing the first profitable year. The VIEs are wholly owned by the Company's employees and controlled by the Company through various contractual agreements. To the extent that the VIEs have undistributed after-tax net income, the Company would have to pay a dividend tax of 20% on behalf of its employees when dividends are distributed from these local entities in the future.

The provisions for income taxes for the three and six months ended June 30, 2006 and 2005 differ from the amounts computed by applying the EIT primarily due to the tax holidays and the preferential tax rate enjoyed by certain of the Company's entities in the PRC. The effective tax rates for the PRC operations for the three and six months ended June 30, 2006 were higher than the same periods of the prior year primarily due to the expiration of tax holidays of certain entities in 2006.

**9. Net Income Per Share**

Basic net income per share is computed using the weighted average number of the ordinary shares outstanding during the period. Diluted net income per share is computed using the weighted average number of ordinary shares and ordinary share equivalents outstanding during the period.

The following table sets forth the computation of basic and diluted net income per share for the periods indicated:

<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>(in thousands, except per share amounts)</b>			

**Basic net income per share calculation:**

Numerator:

Net income used in computing basic net income per share	\$ 10,439	\$ 9,953	\$ 17,475	\$ 20,263
---	-----------	----------	-----------	-----------

Denominator:

Weighted average ordinary shares outstanding	53,554	52,111	53,496	51,771
--	--------	--------	--------	--------

Basic net income per share	\$ 0.19	\$ 0.19	\$ 0.33	\$ 0.39
----------------------------	---------	---------	---------	---------

**Diluted net income per share calculation:**

Numerator:

Net income	\$ 10,439	\$ 9,953	\$ 17,475	\$ 20,263
Amortization of convertible debt issuance cost	171	171	342	342

Net income used in computing diluted net income per share	\$ 10,610	\$ 10,124	\$ 17,817	\$ 20,605
---	-----------	-----------	-----------	-----------

**Table of Contents**

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
	<b>(in thousands, except per share amounts)</b>			
Denominator:				
Weighted average ordinary shares outstanding	53,554	52,111	53,496	51,771
Weighted average ordinary shares equivalents:				
Stock options	1,013	2,795	1,131	2,994
Convertible debt	3,877	3,877	3,877	3,877
Others			18	
Shares used in computing diluted net income per share	58,444	58,783	58,522	58,642
Diluted net income per share	\$ 0.18	\$ 0.17	\$ 0.30	\$ 0.35

**10. Stock-Based Compensation**

The Company's stock option program is a long-term retention program that is intended to attract, retain and incentivize talented employees, officers and directors, and to align stockholder and employee interests. The Company currently grants options pursuant to the 1) 1999 Stock Plan, 2) 1999 Executive Stock Option Plan and 3) 1999 Directors' Stock Option Plan. Prior to August 1, 2005, the Company also offered stock options to its eligible employees pursuant to the 1999 Employee Stock Purchase Plan.

**Stock Compensation**

Effective January 1, 2006, the Company adopted SFAS 123R. See Note 2 for a description of the Company's adoption of SFAS 123R. The fair value of stock-based compensation awards is determined using the Black-Scholes option pricing model, which is consistent with the valuation techniques previously utilized for options in footnote disclosures required under SFAS 123, as amended by FASB Statement No. 148, Accounting for Stock-Based Compensation Transition and Disclosure. The determination of the fair value of stock-based compensation awards on the date of grant using an option-pricing model is affected by the Company's stock price as well as assumptions regarding a number of complex and subjective variables, including the expected volatility of the Company's stock price over the term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate and expected dividends.

The assumptions used to value stock-based compensation awards for the three and six months ended June 30, 2006 and 2005 are as follows:

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Expected term (in years)	3.8-5.0	1.0-4.0	3.8-5.0	1.0-4.0
Expected volatility	67.6%-71.3%	70.0%	67.6%-71.3%	70.0%-87.0%
Risk-free interest rate	5.0%-5.2%	3.9%	5.0%-5.2%	2.9%-3.9%
Expected dividend yield	0	0	0	0

Expected term represents the weighted average period of time that stock-based awards granted are expected to be outstanding giving consideration to historical exercise patterns. Expected volatilities are based on historical volatilities of the Company's ordinary shares. Risk-free rate is based on US Treasury zero-coupon issues with remaining terms similar to the expected term on the stock-based awards. The Company does not anticipate paying any cash dividends in the foreseeable future. Forfeitures are estimated at the time of grant and revised in subsequent periods if actual forfeitures differ from those estimates. The Company uses historical data to estimate pre-vesting option forfeitures and record stock-based compensation expense only for those awards that are expected to vest.

Edgar Filing: SINA CORP - Form 10-Q

Total stock-based compensation recognized on the Company's Condensed Consolidated Statement of Operations for the three and six months ended June 30, 2006 is as follows:

	<b>Three months ended June 30, 2006</b>	<b>Six months ended June 30, 2006</b>
	<b>(in thousands)</b>	
Cost of revenues	\$ 350	\$ 700
Sales and marketing	353	614
Product development	377	711
General and administrative	1,943	2,514
Total	\$ 3,023	\$ 4,539

**Table of Contents**

The following table sets forth the pro forma amounts of net income and net income per share for the three and six months ended June 30, 2005 that would have resulted if the Company had accounted for stock-based awards under the fair value recognition provisions of SFAS 123:

	<b>Three months ended June 30, 2005</b>	<b>Six months ended June 30, 2005 (in thousands)</b>
Net income:		
As reported	\$ 9,953	\$ 20,263
Deduct: Employee stock purchase plan related compensation expenses determined under fair value based method	(45)	(73)
Deduct: Stock-based employee compensation expenses determined under fair value based method	(2,084)	(5,031)
Pro forma	\$ 7,824	\$ 15,159
Basic net income per share:		
As reported	\$ 0.19	\$ 0.39
Pro forma	\$ 0.15	\$ 0.29
Diluted net income per share:		
As reported	\$ 0.17	\$ 0.35
Pro forma	\$ 0.14	\$ 0.26

As of June 30, 2006, there was \$28.4 million of unrecognized compensation cost, adjusted for estimated forfeitures, related to non-vested stock-based awards granted to the Company's employees. This cost is expected to be recognized over a weighted-average period of 2.1 years. Total unrecognized compensation cost may be adjusted for future changes in estimated forfeitures.

**General Stock Option Information**

The following table sets forth the summary of option activity under the Company's stock option program for the six months ended June 30, 2006:

	<b>Options Available for Grant (in thousands, except exercise price)</b>	<b>Options Outstanding</b>	<b>Weighted Average Exercise Price</b>
Beginning of period	2,681	3,610	\$ 14.97
Granted	(2,100)	2,100	\$ 23.90
Exercised	N/A	(157)	\$ 12.36
Cancelled/expired/forfeited	530	(530)	\$ 8.30
End of period	1,111	5,023	\$ 19.49

The total intrinsic value of options exercised for the six months ended June 30, 2006 was \$1.9 million. The intrinsic value is calculated as the difference between the market value as of June 30, 2006 and the exercise price of the shares.

Information regarding the stock options outstanding at June 30, 2006 is summarized below:

<b>Range of Exercise prices</b>	<b>Options Outstanding (in thousands)</b>	<b>Weighted Average Remaining Contractual Life (in years)</b>	<b>Weighted Average Exercise Price</b>	<b>Options Exercisable (in thousands)</b>	<b>Weighted Average Exercise Price</b>
\$0.16 \$1.88	414	5.64	\$ 1.69	382	\$ 1.67
\$1.88 \$12.98	840	6.12	\$ 10.83	614	\$ 10.16
\$12.98 \$20.86	1,024	7.61	\$ 19.79	509	\$ 19.23
\$20.86 \$36.40	2,745	6.56	\$ 24.71	542	\$ 27.92
	5,023	6.63	\$ 19.49	2,047	\$ 15.53

The aggregate intrinsic value of options outstanding and options exercisable as of June 30, 2006 was \$29.4 million and \$21.1 million, respectively.

**Table of Contents****11. Segment Information**

Based on the criteria established by SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, the Company currently operates in three principal business segments globally. The Company does not allocate any operating costs or assets to its advertising, MVAS and other segments as management does not use this information to measure the performance of these operating segments. Management does not believe that allocating these expenses or assets is necessary in evaluating these segments' performance.

The following is a summary of revenues, cost of revenues and gross profit margins:

	<b>Three months ended</b>		<b>Six months ended</b>	
	<b>June 30,</b>		<b>June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
	<b>(in thousands, except percentages)</b>			
<b>Revenues:</b>				
Advertising	\$ 29,454	\$ 20,373	\$ 51,635	\$ 37,021
MVAS	22,448	22,618	45,142	49,133
Other	1,776	3,139	3,613	5,824
	\$ 53,678	\$ 46,130	\$ 100,390	\$ 91,978
<b>Cost of revenues:</b>				
Advertising	\$ 10,317	\$ 6,541	\$ 18,615	\$ 12,435
MVAS	8,925	7,374	18,325	16,044
Other	418	420	765	790
	\$ 19,660	\$ 14,335	\$ 37,705	\$ 29,269
<b>Gross profit margins:</b>				
Advertising	65%	68%	64%	66%
MVAS	60%	67%	59%	67%
Other	76%	87%	79%	86%
Overall	63%	69%	62%	68%

The following is a summary of the Company's geographic operations:

	<b>China</b>	<b>U.S.</b>	<b>Hong Kong</b>	<b>Taiwan</b>	<b>Total</b>
	<b>(in thousands)</b>				
<b>Three months ended and as of</b>					
<b>June 30, 2006:</b>					
Revenue	\$52,812	\$ 469	\$ 303	\$ 94	\$ 53,678
Long-lived assets	21,895	143	1,131	79	23,248
<b>Three months ended and as of</b>					
<b>June 30, 2005:</b>					
Revenues	\$45,122	\$ 515	\$ 363	\$130	\$ 46,130
Long-lived assets	18,950	79	168	375	19,572
<b>Six months ended and as of</b>					
<b>June 30, 2006:</b>					
Revenue	\$98,551	\$1,002	\$ 647	\$190	\$100,390
Long-lived assets	21,895	143	1,131	79	23,248



**Six months ended and as of  
June 30, 2005:**

Revenues	\$89,845	\$1,048	\$ 807	\$278	\$ 91,978
Long-lived assets	18,950	79	168	375	19,572

**12. Certain risks and concentrations**

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of cash and cash equivalents, marketable debt securities and accounts receivable. The Company limits its exposure to credit loss by depositing its cash and cash equivalents with financial institutions in the U.S., the PRC, Hong Kong and Taiwan that management believes are of high credit quality. The Company usually invests in marketable debt securities with A ratings or above.

Accounts receivable consist primarily of advertising agencies, direct advertising customers and third-party mobile operators. As of June 30, 2006 and December 31, 2005, approximately 98% and 97%, respectively, of the net accounts receivable were derived from the Company's operations in the PRC. With regard to the advertising operations, no individual advertising customer accounted for more than 10% of total net revenues for the three and six months ended June 30, 2006 and 2005. Also, no individual advertising customer accounted for more than 10% of accounts receivables as of June 30, 2006 and December 31, 2005. With regard to the

**Table of Contents**

MVAS operations, the Company mainly contracts with China Mobile Communication Corporation ( China Mobile ) and China Unicom Co. Ltd. ( China Unicom ) and their subsidiaries for utilizing their transmission gateways for message delivery and billing systems to collect subscription or usage fees from its subscribers. MVAS fees charged to users via these operators accounted for 42% and 45% of the Company's net revenues for the three and six months ended June 30, 2006, respectively, and 49% and 54% of the Company's net revenues for the three and six months ended June 30, 2005, respectively. Short Messaging Service ( SMS ) revenue accounted for 30% and 32% of the Company's net revenues for the three and six months ended June 30, 2006, respectively, and 34% and 39% of the Company's net revenues for the three and six months ended June 30, 2005, respectively. Accounts receivable from the mobile operators represent MVAS fees collected on behalf of the Company after deducting their billing services and transmission charges. The Company maintains allowances for potential credit losses. Historically, the Company has not had any significant direct write-off of bad debts.

Revenues received through China Mobile and its subsidiaries accounted for 33% and 37% of the Company's total net revenues for the three and six months ended June 30, 2006, respectively, and 44% and 47% of the Company's total net revenues for the three and six months ended June 30, 2005, respectively. It also accounted for 34% and 26% of the Company's total accounts receivable as of June 30, 2006 and December 31, 2005, respectively.

The Company operates in business segments which are characterized by rapid technological advances, changes in customer requirements and evolving regulatory requirements and industry standards. Any failure by the Company to anticipate or to respond adequately to technological changes in its industry segments, changes in customer requirements or changes in regulatory requirements or industry standards, could have a material adverse effect on the Company's business and operating results. The Company relies on a number of third-party suppliers for various other services, including web server hosting, banner advertising delivery software, Internet traffic measurement software and transmission and billing of MVAS. Any failure of these suppliers to provide services to the Company or any termination of these services with the Company could have a material adverse effect on the Company's business and operating results.

The majority of the Company's net income was derived from China. The operations in China are carried out by the Company's subsidiaries and VIEs. The Company depends on dividend payments from its subsidiaries in China for its revenues after these subsidiaries receive payments from VIEs in China under various services and other arrangements. In addition, under Chinese law, its subsidiaries are only allowed to pay dividends to the Company out of their accumulated profits, if any, as determined in accordance with Chinese accounting standards and regulations. Moreover, these Chinese subsidiaries are required to set aside at least 10% of their respective accumulated profits, if any, up to 50% of their registered capital to fund certain mandated reserve funds that are not payable or distributable as cash dividends. The appropriation to mandated reserve funds are assessed annually. As of December 31, 2005, the Company is subject to a maximum appropriation of \$11.1 million to these non-distributable reserve funds. The Company's subsidiaries and VIEs in China are subject to different tax rates. See Note 8 Income Taxes.

The majority of the Company's revenues derived and expenses incurred were in Chinese renminbi. As of June 30, 2006, the Company's cash, cash equivalents and short-term investments balance denominated in Chinese renminbi was approximately \$207.3 million, which accounted for approximately 66% of its total cash, cash equivalents and short-term investment balance; accounts receivable denominated in Chinese renminbi was approximately \$47.4 million, which accounted for approximately 98% of its total accounts receivable balance; and liabilities balance denominated in Chinese renminbi was approximately \$40.3 million, which accounted for approximately 28% of its total liabilities balance. Accordingly, the Company may experience economic losses and negative impacts on earnings and equity as a result of exchange rate fluctuations in renminbi. Moreover, the Chinese government imposes controls on the convertibility of renminbi into foreign currencies and, in certain cases, the remittance of currency out of the PRC. The Company may experience difficulties in completing the administrative procedures necessary to obtain and remit foreign currency.

**13. Commitments and Contingencies**

Operating lease commitments include the commitments under the lease agreements for the Company's office premises. The Company leases office facilities under non-cancelable operating leases with various expiration dates beginning 2005 through 2007. Rental expenses for the three and six months ended June 30, 2006 were \$0.8 million

and \$1.6 million, respectively, and for the three and six months ended June 30, 2005 were \$1.0 million and \$1.9 million, respectively. Based on the current rental lease agreements, future minimum rental payments required as of June 30, 2006 were as follows:

**Table of Contents**

	<b>Total</b>	<b>Less than one year</b>	<b>One to three years</b>	<b>Three to five years</b>	<b>More than five years</b>
		<b>( in thousands)</b>			
Operating lease commitments	\$2,819	\$ 2,338	\$ 481	\$	\$

Purchase commitments mainly include minimum commitments for Internet connection fees associated with web sites production, content fees associated with web sites production and MVAS, advertising serving services and marketing activities. Purchase commitments as of June 30, 2006 were as follows:

	<b>Total</b>	<b>Less than one year</b>	<b>One to three years</b>	<b>Three to five years</b>	<b>More than five years</b>
		<b>( in thousands)</b>			
Purchase commitments	\$13,723	\$ 10,593	\$3,012	\$46	\$ 72

There are uncertainties regarding the legal basis of our ability to operate an Internet business and value-added telecommunication services in China. Although the country has implemented a wide range of market-oriented economic reforms, the telecommunication, information and media industries remain highly regulated. Not only are such restrictions currently in place, but in addition regulations are unclear as to in which specific segments of these industries companies with foreign investors, including us, may operate and the manner of any such operations. Therefore, we might be required to limit the scope of our operations in China or alter the manner in which we operate, or both and any such operational changes could have a material adverse effect on our financial position, results of operations and cash flows.

For a discussion of current lawsuits, please refer to Part II, Item 1. *Legal Proceedings*.

**14. Subsequent Event**

In July 2006, China Mobile made significant changes to their policy on subscription-based MVAS, which included extending the trial period and requiring double reminders on new MVAS subscriptions as well as sending SMS reminders to existing monthly subscribers of SMS, MMS and WAP to inform them of their MVAS subscription and fee information. These policy changes could have a significant and adverse impact on the Company's MVAS business going forward. For the three months ending September 30, 2006, the Company may need to assess the goodwill and intangible assets related to the MVAS business for impairment. As of June 30, 2006, total goodwill and intangible assets related to the MVAS business was \$69.4 million.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Exchange Act, including, without limitation, statements regarding our expectations, beliefs, intentions or future strategies that are signified by the words expect, anticipate, intend, believe, the negative of such terms or other comparable terminology. All forward-looking statements included in this document are based on information available to us on the date hereof, and we undertake no obligation to update any such forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. In evaluating our business, you should carefully consider the information set forth in the section titled Risk Factors in Part II, Item 1A. We caution you that our businesses and financial performance are subject to substantial risks and uncertainties, including the factors identified in Risk Factors, that could cause actual results to differ materially from those in the forward-looking statements.*

**Overview**

We are a leading online media company and value-added information services provider in the People's Republic of China (the PRC or China) and the global Chinese communities. With a branded network of localized web sites targeting Greater China and overseas Chinese, we provide services through five major business lines including

SINA.com (online news and content), SINA Mobile (MVAS), SINA Online (community-based services, games and instant messaging), SINA.net (search and enterprise solutions) and SINA E-Commerce (online shopping). Together these provide an array of services including region-focused online portals, MVAS, search and directory, interest-based and community-building channels, free and premium email, audio and video streaming, online games, virtual ISP, classified listings, fee-based services, e-commerce and enterprise e-solutions. In turn, we generate revenues through advertising, MVAS, fee-based services, e-commerce and enterprise services. Advertising and MVAS are currently the major sources of our revenues and we expect this trend to continue in the near future.

**Table of Contents****Critical Accounting Policies and Estimates**

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles in the United States of America ( GAAP ). The preparation of these financial statements requires us to make estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to customer programs and incentives, bad debts, investments, intangible assets, income taxes, financing operations, restructuring, employee benefits, contingencies and litigation. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. For further information on our critical accounting policies, see the discussion in the section titled Recent Accounting Pronouncements below and Note 2 to the Condensed Consolidated Financial Statements.

Other than noted below, there have been no significant changes during the first half of 2006 to the items disclosed as our critical accounting policies and estimates in the Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2005.

***Stock-based compensation***

We adopted the provisions of, and account for stock-based compensation in accordance with, SFAS 123R during the first quarter of fiscal 2006. We elected the modified-prospective method, under which prior periods are not revised for comparative purposes. Under the fair value recognition provisions of SFAS 123R, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis (net of estimated forfeitures) over the requisite service period, which generally is the vesting period. We currently use the Black-Scholes option pricing model to determine the fair value of stock options and ESPP shares. The determination of the fair value of stock-based compensation awards on the date of grant using an option-pricing model is affected by our stock price as well as assumptions regarding a number of complex and subjective variables, including our expected stock price volatility over the term of the awards, actual and projected employee stock option exercise behaviors, risk-free interest rate and expected dividends. Furthermore, we are required to estimate forfeitures at the time of grant and record stock-based compensation expense only for those awards that are expected to vest. If actual forfeitures differ from those estimates, we may need to revise those estimates in subsequent periods.

If factors change and we employ different assumptions for estimating stock-based compensation expense in future periods or if we decide to use a different valuation model, the future periods may differ significantly from what we have recorded in the current period and could materially affect our operating income, net income and net income per share.

The Black-Scholes option-pricing model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable, characteristics not present in our option grants and ESPP shares. Existing valuation models, including the Black-Scholes and lattice binomial models, may not provide reliable measures of the fair values of our stock-based compensation. Consequently, there is a risk that our estimates of the fair values of our stock-based compensation awards on the grant dates may bear little resemblance to the actual values realized upon the exercise, expiration, early termination or forfeiture of those stock-based payments in the future. Certain stock-based compensation awards, such as employee stock options, may expire worthless or otherwise result in zero intrinsic value as compared to the fair values originally estimated on the grant date and reported in our financial statements. Alternatively, value may be realized from these instruments that are significantly higher than the fair values originally estimated on the grant date and reported in our financial statements. There currently is no market-based mechanism or other practical application to verify the reliability and accuracy of the estimates stemming from these valuation models, nor is there a means to compare and adjust the estimates to actual values.

The guidance provided in SFAS 123R and SAB 107 is relatively new. The application of these principles may be subject to further interpretation and refinement over time. There are significant differences among valuation models, and there is a possibility that we will adopt different valuation models in the future. This may result in a lack of consistency in future periods and materially affect the fair value estimates of stock-based compensation awards. It

may also result in a lack of comparability with other companies that use different models, methods and assumptions.  
See Note 10 for further information regarding stock-based compensation under SFAS 123R.

**Table of Contents****Property and equipment**

Property and equipment are stated at historical cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally from three to five years. Judgment is required to determine the estimated useful lives of assets, especially for computer equipment, including determining how long existing equipment can function and when new technologies will be introduced at cost-effective price points to replace existing equipment. Changes in these estimates and assumptions could materially impact our financial position and results of operations.

During a recent fixed-assets inventory count, we noted that a significant portion of certain fully depreciated computer equipment was still in use. We changed the estimated useful lives of these computer equipment (e.g., servers and filers), from three years to four years. This change in accounting estimate resulted in a reduction in depreciation expenses of \$0.6 million in the first quarter of 2006, of which \$0.2 million were in the cost of advertising revenues and \$0.4 million were in operating expenses. Depreciation expenses were approximately \$2.4 million and \$4.7 million for the three and six months ended June 30, 2006, respectively, and \$2.2 million and \$4.2 million for the three and six months ended June 30, 2005, respectively.

**Recent Accounting Pronouncements**

In July 2006, the Financial Accounting Standards Board ( FASB ) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 ( FIN 48 ), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that we recognize in our financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective for us on January 1, 2007, with the cumulative effect of the change in accounting principle, if any, recorded as an adjustment to opening retained earnings. We are currently evaluating the impact of adopting FIN 48 on our consolidated financial position, cash flows and results of operations.

**Results of Operations****Net revenues**

	Three months ended June 30,				% of change	
	2006	2005				
	(in thousands, except percentages)		% of net revenues	% of net revenues		
Net Revenues:						
Advertising	\$ 29,454		55%	\$ 20,373	44%	45%
Non-advertising:						
MVAS	22,448		42%	22,618	49%	-1%
Other	1,776		3%	3,139	7%	-43%
Subtotal	24,224		45%	25,757	56%	-6%
Total net revenues	\$ 53,678		100%	\$ 46,130	100%	16%

	Six months ended June 30,				% of change
	2006	2005			
	(in thousands, except percentages)		% of net revenues	% of net revenues	



Edgar Filing: SINA CORP - Form 10-Q

Net Revenues:					
Advertising	\$ 51,635	51%	\$ 37,021	40%	39%
Non-advertising:					
MVAS	45,142	45%	49,133	54%	-8%
Other	3,613	4%	5,824	6%	-38%
Subtotal	48,755	49%	54,957	60%	-11%
Total net revenues	\$ 100,390	100%	\$ 91,978	100%	9%

During the second quarter and first half of 2006, total net revenues increased by \$7.5 million, or 16%, and \$8.4 million, or 9%, respectively, compared to the same periods of 2005. Advertising revenues in absolute dollars and as a percentage of total net revenues grew while MVAS revenues declined.

*Advertising.* The year-over-year growth in advertising revenues in the second quarter and first half of 2006 was primarily due to

**Table of Contents**

the increase in the number of advertisers, price and overall average spending per advertiser in China. Compared to the same periods last year, the advertising revenue growth in the second quarter and first half of 2006 came mostly from the automobile, real estate and information technology sectors and was boosted by the World Cup event. Since many of our advertisers for the World Cup are recurring customers who regularly advertise with us even in the absence of the World Cup event, we are unable to quantify the incremental revenues that can attributed solely to the World Cup event.

During the second quarter and first half of 2006, China accounted for 98% and 97% of our total advertising revenues, respectively, compared to 96% and 95% in the same periods of 2005, respectively. Average spending per advertising customer in the PRC grew from \$54,100 and \$70,000 in the second quarter and first half of 2005, respectively, to \$55,800 and \$76,000 in the second quarter and first half of 2006, respectively. Our top ten customers in aggregate generated 27% and 16% of our advertising revenues during the second quarter and first half of 2006, respectively, compared to 15% and 17% in the same periods of 2005.

*Non-advertising.* The year-over-year decline in non-advertising revenues in the second quarter of 2006 can be mostly attributed to the 43% decline in other (non-MVAS related) non-advertising revenues. The year-over-year decline in non-advertising revenues in the first half of 2006 was due to a decline of 8% in MVAS revenues and a decline of 38% in other non-advertising revenues.

**MVAS**

	<b>Three months ended June 30,</b>				
	<b>2006</b>	<b>2005</b>		<b>% of change</b>	
		<b>(in thousands, except percentages)</b>			
2.0G products	\$ 18,653	83%	\$ 18,999	84%	-2%
2.5G products	3,795	17%	3,619	16%	5%
Total MVAS revenues	\$ 22,448	100%	\$ 22,618	100%	-1%

	<b>Six months ended June 30,</b>				
	<b>2006</b>	<b>2005</b>		<b>% of change</b>	
		<b>(in thousands, except percentages)</b>			
2.0G products	\$ 37,974	84%	\$ 41,774	85%	-9%
2.5G products	7,168	16%	7,359	15%	-3%
Total MVAS revenues	\$ 45,142	100%	\$ 49,133	100%	-8%

Revenues from 2.0G products, which includes SMS, interactive voice response system ( IVR ) and color ringbacktone ( CRBT ), decreased 2% and 9% year-over-year in the second quarter and first half of 2006, respectively. Revenues from SMS were \$16.1 million and \$15.6 million in the second quarter of 2006 and 2005, respectively, and accounted for 72% and 69% of total MVAS revenues over the respective periods. For the first half of 2006, SMS revenues declined \$3.7 million, or 10%, year-over-year, which was largely due to higher churn rates by our monthly subscription users and less effective means to recruit new users. SMS revenues accounted for 71% and 73% of total MVAS revenues in the first half of 2006 and 2005, respectively. Revenues from CRBT decreased 58% and 39% year-over-year in the second quarter and first half of 2006, respectively. Revenues from IVR grew 2% and 22% year-over-year in the second quarter and first half of 2006, respectively, primarily due to the addition of IVR service with China Telecom.

On a year-over-year basis, revenues from 2.5G products, including multimedia messaging service ( MMS ), wireless application protocol ( WAP ) and Kjava, increased 5% in the second quarter of 2006 but decreased 3% in the first half of 2006. MMS declined 45% in the second quarter and 51% for the first half of 2006. These year-over-year decreases were partially offset by the year-over-year increase in WAP and Kjava revenues. The year-over-year decreases in MMS revenues were mainly related to the termination of MMS Album by China Mobile and the new billing platform, which have made new user recruitment more difficult and increased the failure rate on fee collection from our users.

In July 2006, China Mobile made significant changes to their policy on subscription-based MVAS. These changes were in accordance with policy directives from China's Ministry of Information Industry ( MII ) and were intended to address a number of issues, including reducing subscriber complaints, increasing customer satisfaction and promoting healthy development of the MVAS industry in China. The key changes include extending the trial period and requiring double reminders on new MVAS subscriptions as well as sending SMS reminders to existing monthly subscribers of SMS, MMS and WAP to inform them of their MVAS subscription and fee information. Certain provincial subsidiaries, such as Guangdong Mobile, one of China Mobile's largest provincial

**Table of Contents**

subsidiaries, have begun to discontinue charging MVAS users monthly subscription fees unless the users reply to the SMS reminders and reconfirm their subscription. Other provincial subsidiaries are expected to announce similar measures of their own. In addition, it is expected that China Mobile's provincial subsidiaries will begin canceling existing WAP subscriptions that have been inactive for the prior four months and existing SMS subscriptions of users who have not successfully received more than three SMS messages during the month. These policy changes from China Mobile will reduce our ability to acquire new monthly MVAS subscribers and increase the churn rate of our existing monthly MVAS subscribers. Although we have not completed our assessment of the policy changes, we believe that these changes could have a significant, adverse impact on our results of operations, cash flow and financial condition going forward. Other Chinese mobile operators, like China Unicom, may announce measures in response to the MII campaign. For the second quarter of 2006, 42% of our revenues were from the MVAS business, approximately 67% of which related to monthly subscription from China Mobile. Since we derive the majority of our China Mobile subscription revenues from SMS, MMS and WAP, we expect revenues from these products to be negatively impacted going forward. We are in the process of developing new products, such as IVR, that are not subject to China Mobile's recent policy changes. However, there is no guarantee that we will be able to develop any such new products, that any such products will achieve market acceptance or that such products will not be affected by future rules and regulations.

**Other non-advertising revenues**

Other non-advertising revenues include fee-based services, such as virtual ISP and paid email services, e-commerce and other enterprise services such as paid search and directory listings. The year-over-year decreases in other non-advertising revenues in the second quarter and first half of 2006 were due to revenue declines from paid search and directory listings, loss of revenues from the sale of our online hotel-booking business in the third quarter of 2005 and the sale of our interest in an online auction joint venture in the fourth quarter of 2005.

Revenues from paid search and directory listings accounted for 55% and 61% of our other non-advertising revenues in the second quarter and first half of 2006, respectively. These revenues are generated mainly from pay-by-listing products offered on our old search platform. Starting in the first quarter of 2006, we began to promote our new search engine iAsk as the preferred search engine on our website. iAsk is currently being offered free of charge. Consequently, we expect revenues from paid search and directory listings to continue to decline as existing contracts expire.

**Cost of revenues**

	<b>Three months ended June 30,</b>		
	<b>2006</b>	<b>2005</b>	<b>% of Change</b>
	<b>(in thousands, except percentages)</b>		
Cost of revenues:			
Advertising	\$ 10,317	\$ 6,541	58%
Non-advertising:			
MVAS	8,925	7,374	21%
Other	418	420	*
Subtotal	9,343	7,794	20%
Total cost of revenues	\$ 19,660	\$ 14,335	37%

	<b>Six months ended June 30,</b>		
	<b>2006</b>	<b>2005</b>	<b>% of Change</b>
	<b>(in thousands, except percentages)</b>		

Edgar Filing: SINA CORP - Form 10-Q

Cost of revenues:			
Advertising	\$ 18,615	\$ 12,435	50%
Non-advertising:			
MVAS	18,325	16,044	14%
Other	765	790	-3%
Subtotal	19,090	16,834	13%
Total cost of revenues	\$ 37,705	\$ 29,269	29%

\* Less than 1%

Compared to last year, cost of revenues increased 37% in the second quarter and 29% in the first half of 2006. This was primarily due to the increase in cost of revenues from our advertising and MVAS businesses.

*Advertising.* Cost of advertising revenues consist mainly of expenses associated with the production of our web sites, which include fees paid to third parties for Internet connection, content and services, personnel related costs and equipment depreciation expenses associated with our web site production. Cost of advertising revenues also includes the business taxes on advertising sales in

**Table of Contents**

the PRC. Business taxes levied on advertising sales are approximately 8.5% of the advertising revenues.

The year-over-year increases of 58% and 50% in cost of advertising revenues in the second quarter and first half of 2006, respectively, were primarily due to the increase in web production costs driven by an increase in web production personnel and content fees, the increase in Internet connection costs associated with the additional bandwidth as well as the increase in business taxes associated with higher advertising revenues. These increases were driven by the need to provide additional resources to support our web traffic and advertising revenue growth. Upon the adoption of SFAS 123R on January 1, 2006, cost of advertising revenues in the second quarter and first half of 2006 also included stock-based compensation of \$0.4 million and \$0.7 million, respectively.

*Non-advertising.* Cost of non-advertising revenues consists mainly of fees paid to third-party mobile operators for their services relating to the collection of our MVAS revenues and for using their transmission gateways, fees or royalties paid to third-party content providers for services and content associated with our MVAS, and costs for providing our enterprise services. Cost of non-advertising revenues also includes business taxes levied on non-advertising sales in the PRC. Business taxes levied on MVAS are at 3% for mobile related revenues and at 5% for other non-advertising revenues.

Compared to last year, cost of MVAS revenues increased 21% in the second quarter and 14% in the first half of 2006. The year-over-year increases were mostly due to the increase in royalties paid to third-party content providers and the increase in fees retained by or paid to mobile operators. Fees paid to third-party content providers for the second quarter of 2006 and 2005 were \$1.9 million and \$1.1 million, respectively, or 9% and 5% of our MVAS revenues, respectively, and \$4.2 million and \$2.8 million for the first half of 2006 and 2005, respectively, or 9% and 6% of our MVAS revenues, respectively. Fees retained by or paid to mobile operators for the second quarter of 2006 and 2005 were \$6.5 million and \$5.6 million, respectively, or 29% and 25% of our MVAS revenues, respectively, and \$13.1 million and \$12.0 million in the first half of 2006 and 2005, respectively, or 29% and 25% of our MVAS revenues, respectively.

Under certain renewed arrangements with China Unicom, the service fee that China Unicom charges has been revised to a flat rate of 20% of the fees we charge to our users. Historically, service fees from China Unicom were set based on the volume of business with the mobile operator and mainly fluctuated between 10 - 40%, depending on the period and arrangement, but typically were around 12%. In July 2005, China Mobile introduced a three-tier scheme to revenue sharing on new arrangements. Under the new scheme, China Mobile charges 15% for using only its billing services, 30% for using its billing and customer support services and 50% for using its billing, customer support and marketing services. We currently do not rely on China Mobile for customer support and marketing services. However, if we choose to or are required to use China Mobile's customer support or marketing services in the future, our operating margin for MVAS will be negatively impacted. China Mobile and China Unicom may choose to further increase the fees charged for providing their services, which may have a material adverse impact on our results of operations. For these reasons, historical cost trends may not be indicative of future results.

**Gross profit margins**

	<b>Three months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>
Gross profit margins:		
Advertising	65%	68%
Non-advertising:		
MVAS	60%	67%
Other	76%	87%
Subtotal	61%	70%
Overall	63%	69%
	<b>Six months ended June 30,</b>	

	<b>2006</b>	<b>2005</b>
Gross profit margins:		
Advertising	64%	66%
Non-advertising:		
MVAS	59%	67%
Other	79%	86%
Subtotal	61%	69%
Overall	62%	68%

**Table of Contents**

Overall gross profit margin for both the second quarter and first half of 2006, declined 6% from the same periods of 2005.

*Advertising.* The year-over-year decreases in advertising gross profit margin in the second quarter and first half of 2006 were primarily due to the increased investment in our website production and stock-based compensation, which we began to expense starting January 1, 2006, pursuant to SFAS 123R. Stock-based compensation for the second quarter and the first half of 2006 accounted for approximately 1% of our advertising revenues.

*Non-advertising.* The majority of the costs associated with non-advertising revenues are variable costs. The year-over-year decreases in non-advertising gross profit margin for the second quarter and first half of 2006 were mainly driven by the increase in transmission cost and content cost without a proportionate increase in revenues from MVAS. We expect a further increase in fees paid to mobile operators and content providers as a percentage of MVAS revenues, which would result in a continuing decline in MVAS gross profit margin in the near future.

**Operating expenses**

	Three months ended June 30,				% of change
	2006	2005			
	(in thousands, except percentages)				
		% of total net		% of total net	
		Revenues		revenues	
Sales and marketing expenses	\$ 13,497	25%	\$ 10,718	23%	26%
Product development expenses	\$ 4,993	9%	\$ 3,520	8%	42%
General and administrative expenses	\$ 7,427	14%	\$ 5,078	11%	46%

	Six months ended June 30,				% of change
	2006	2005			
	(in thousands, except percentages)				
		% of total net		% of total net	
		Revenues		revenues	
Sales and marketing expenses	\$ 25,302	25%	\$ 22,202	24%	14%
Product development expenses	\$ 9,603	10%	\$ 7,222	8%	33%
General and administrative expenses	\$ 12,584	13%	\$ 9,775	11%	29%

*Sales and marketing expenses.* Sales and marketing expenses consist primarily of compensation expenses, sales commissions, advertising and promotion expenditures and travel expenses. The year-over-year increases in sales and marketing expenses in absolute dollars and as a percentage of total net revenues for the second quarter and first half of 2006 were primarily due to increased advertising and promotion for our World Cup-related content, which was approximately \$1.2 million. Sales and marketing expenses also increased from the prior year as a result of increased promotion for our MVAS products and increased personnel-related expenses, such as commissions. Sales and marketing expenses in the second quarter and first half of 2006 also included stock-based compensation of \$0.4 million and \$0.6 million, respectively, as a result of adopting SFAS 123R on January 1, 2006.

*Product development expenses.* Product development expenses consist primarily of personnel related expenses incurred for enhancement to and maintenance of our web sites as well as costs associated with new product development such as email and search engine products. The year-over-year increases for the second quarter and first half of 2006 in absolute dollars and as a percentage of total net revenues were primarily due to an increase in headcount and depreciation expenses resulting from additional purchases of capital equipment. Product development



expenses in the second quarter and first half of 2006 also included stock-based compensation of \$0.4 million and \$0.7 million, respectively, as a result of adopting SFAS 123R. We expect our product development expenses to continue to increase in absolute dollars in the near future.

*General and administrative expenses.* General and administrative expenses consist primarily of compensation for personnel, fees for professional service, and provisions for doubtful accounts. Our general and administrative expenses also include expenses relating to the transfer of the economic benefits generated from our VIEs in the PRC to our subsidiaries. The year-over-year increases in absolute dollars and as a percentage of total net revenues for the second quarter and first half of 2006 were mainly due to the increase in provision for doubtful accounts as a result of increased advertising revenues. Other increases for the second quarter and first half of 2006 included \$0.4 million and \$0.6 million, respectively, related to the transfer of economic benefits generated from our VIEs in the PRC to our subsidiaries. General and administrative expenses in the second quarter and first half of 2006 also included stock-based compensation of \$1.9 million and \$2.5 million, respectively, as a result of adopting SFAS 123R. Second quarter stock-based compensation included an expense of \$1.2 million related to option shares granted to directors with immediate vesting. During the

**Table of Contents**

second quarter and first half of 2005, we incurred certain non-recurring expenses, \$0.5 million and \$1.2 million in professional fees, respectively, in relation to our adoption of a shareholder rights plan and \$0.2 million related to the consolidation of our facilities in Beijing in the first quarter of 2005.

**Amortization of intangible assets.**

Amortization of intangibles for the second quarter and first half of 2006 were approximately \$0.5 million and \$0.9 million, respectively, or 1% of total net revenues, compared with \$1.0 million and \$2.1 million, or 2% of total net revenues, over the same periods of 2005. As of June 30, 2006, the net carrying amount of our intangible assets includes mainly purchased technology and non-competition agreements. These intangible assets are amortized over their respective useful lives. See Note 6 to the Condensed Consolidated Financial Statements for further information on intangible assets, including estimates of amortization expenses for future periods.

**Interest and other income**

Interest income grew to \$2.0 million in the second quarter of 2006 from \$1.6 million in the same period last year. For the first half of 2006, interest income was \$3.9 million compared to \$3.1 million in the same period last year. The year-over-year increases were due to higher balance of cash, cash equivalent and short-term investments as well as higher interest rates.

**Amortization of convertible debt issuance cost**

As a result of our sale of zero coupon convertible subordinated notes in July 2003, we recorded convertible debt issuance cost of approximately \$2.7 million, which is being amortized over four years. The amortization expense was \$0.2 million for the second quarter of each of 2006 and 2005 and \$0.3 million for first half of 2006 and 2005.

**Loss on equity investments**

The following summarizes the net loss on our equity investments:

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
	<b>(in thousands, except percentages)</b>			
Shanghai NC SINA *	\$	\$ (46)	\$ (108)	\$ 257
COAL **		(629)		(1,498)
Others	(162)	(183)	(397)	(183)
	\$ (162)	\$ (858)	\$ (505)	\$ (1,424)
% of total net revenues	<(1%)	(2%)	(1%)	(2%)

\* During the three months ended June 30, 2006, we sold our 51% interest in Shanghai NC SINA, a joint venture with NC Soft, and we recorded a gain of \$2.0 million from this transaction.

\*\*

During the three months ended December 31, 2005, we sold our 33% interest in COAL (a.k.a. 1Pai.com), an online auction joint venture with Yahoo! Inc., to Alibaba.com.

***Provision for income taxes***

	Three months ended		Six months ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
	(in thousands, except percentages)			
Income tax provision	\$878	\$682	\$1,683	\$1,213
Effective tax rate for China operation	7%	5%	7%	4%

Based on our current operating structure and preferential tax treatments available to us in China, we expect our effective income tax rate for our China operation to be between 5% to 10% in 2006. The increases in effective income tax rate from the same periods last year were primarily due to the expiration of tax holidays for certain entities in China. For further information on our tax structures and inherent risks see [If tax benefits currently available to us in China were no longer available, our effective income tax rates for our China operations could increase to 33%](#) under Risk Factors in Part II Item 1A. See also Note 8 [Income Taxes](#) to the Condensed Consolidated Financial Statements for further discussion on income taxes.

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

	<b>As of June 30,</b>	
	<b>2006</b>	<b>2005</b>
	<b>(in thousands)</b>	
Cash, cash equivalents and short-term investments	\$312,481	\$284,132
Working capital	\$324,122	\$285,525
Shareholder's equity	\$344,393	\$288,438

We have funded our recent operations and capital expenditures primarily using the \$97.5 million raised through the sale of preference shares, the \$68.8 million raised from the sale of ordinary shares in the initial public offering and the \$97.3 million raised from the sale of zero coupon convertible subordinated notes in July 2003 as well as net income from our operations.

As of June 30, 2006, we had \$312.5 million in cash, cash equivalents and short-term investments to meet the future requirements of our operating activities. We believe that our existing cash, cash equivalents and short-term investments will be sufficient to fund our operating activities, capital expenditures and other obligations for at least the next twelve months. However, we may sell additional equities or obtain credit facilities to enhance our liquidity position or increase our cash reserve for future acquisitions. The sale of additional equity would result in further dilution to our shareholders. The incurrence of indebtedness would result in increased fixed obligations and could result in operating covenants that would restrict our operations. We cannot guarantee that financing will be available in amounts or on terms acceptable to us, if at all.

The following table sets forth the movements of our cash and cash equivalents for the periods presented:

	<b>Six months ended June 30,</b>	
	<b>2006</b>	<b>2005</b>
	<b>(in thousands)</b>	
Net cash provided by operating activities	\$ 20,571	\$ 30,838
Net cash provided by (used in) investing activities	5,257	(26,010)
Net cash provided by financing activities	1,938	4,965
Effect of exchange rate changes on cash and cash equivalents	540	
Net increase in cash and cash equivalents	28,306	9,793
Cash and cash equivalents at beginning of period	88,410	153,768
Cash and cash equivalents at end of period	\$ 116,716	\$ 163,561

***Operating activities***

Net cash provided by operating activities for the six months ended June 30, 2006 was \$20.6 million. This was primarily attributable to our net income of \$17.5 million, adjusted by non-cash related expenses of \$11.1 million and a net decrease in working capital of \$8.0 million. The decrease in working capital was mainly due to an increase in accounts receivable of \$12.5 million, which mostly resulted from World Cup-related revenues that were generated in June 2006, offset by an increase in accrued liabilities of \$4.5 million.

Net cash provided by operating activities for the six months ended June 30, 2005 was \$30.8 million. Net cash provided by operating activities was primarily attributable to our net income of \$20.3 million, adjusted by non-cash related expenses of \$9.8 million and a net increase in working capital items of \$0.7 million. The increase in working capital was mainly due to a decrease in accounts receivable of \$7.2 million, which mainly resulted from improved collection, offset by a decrease in accrued liabilities of \$6.7 million which was primarily due to the decrease in accrual for sales rebates, payroll withholding tax and customer advances.

The year-over-year decrease in net cash provided by operating activities for the six months ended June 30, 2006, was primarily attributable to lower working capital generated and lower net income.

***Investing activities***

Net cash provided by investing activities for the six months ended June 30, 2006 was \$5.3 million. This was primarily generated from the sale of short-term investments of \$16.5 million and from the sales of our interests in an online auction joint venture, online game joint venture and online travel business totaling \$5.6 million, offset by additional consideration paid for the Crillion acquisition of \$11.3 million and equipment purchases of \$5.5 million.

Net cash used in investing activities for the six months ended June 30, 2005 was \$26.0 million. This was primarily related to

**Table of Contents**

additional consideration paid for the Crillion acquisition of \$16.9 million, investment in capital spending of \$7.8 million and investments in joint ventures of \$2.8 million, offset by proceeds from the sale of investments totaling \$1.5 million.

***Financing activities***

Net cash provided by financing activities for the six months ended June 30, 2006 and 2005 were \$1.9 million and \$5.0 million, respectively, both primarily representing the proceeds from the exercise of stock options.

**Contractual Obligations**

As of June 30, 2006, our contractual obligations consisted of long-term debt obligations, operating lease obligations, purchase obligations and other contractual obligations. Long-term debt obligations represent the \$100 million zero-coupon convertible subordinated notes issued on July 7, 2003. Operating lease obligations relate to our facilities in the PRC, as well as in the U.S., Taiwan and Hong Kong. Purchase obligations mainly include the commitments for Internet connection fees associated with website production, content fees associated with website production and MVAS, advertising serving services and marketing activities. As of June 30, 2006, operating lease commitments totaled \$2.8 million and purchase obligations totaled \$13.7 million. For additional information on operating lease obligations, purchase obligations and other contractual obligations, see Note 13 Commitments and contingencies to the Condensed Consolidated Financial Statements.

**Off-Balance Sheet Commitments and Arrangements**

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

**Item 3. Quantitative and Qualitative Disclosures about Market Risk****Interest Rate and Security Market Risk**

Our investment policy limits our investments of excess cash to government or quasi-government securities and in high-quality corporate securities and limits the amount of credit exposure to any one issuer. We protect and preserve our invested funds by limiting default, market and reinvestment risk. Due to the fact that a majority of our investments are in short-term instruments, we believe that the Company has the ability to hold to maturity these investments. As of June 30, 2006 we had unrealized losses of \$4.2 million related to our short-term investments included in accumulated other comprehensive loss in shareholders' equity.

Our zero coupon convertible subordinated notes due 2023, which were issued in July 2003 in the amount of \$100 million, bear no interest and are denominated in U.S. dollars and therefore there is no interest or foreign currency exchange risk associated with the outstanding notes.

**Foreign Currency Exchange Rate Risk**

The majority of our revenues derived and expenses and liabilities incurred are in Chinese renminbi with a relatively small amount in New Taiwan dollars, Hong Kong dollars and U.S. dollars. Thus, our revenues and operating results may be impacted by exchange rate fluctuations in the currencies of China, Taiwan and Hong Kong. See Currency fluctuations and restrictions on currency exchange may adversely affect our business, including limiting our ability to convert Chinese renminbi into foreign currencies and, if Chinese renminbi were to decline in value, reducing our revenue in U.S. dollar terms under Part II Item 1A. *Risk Factors*. We have not reduced our exposure to exchange rate fluctuations by using hedging transactions. While we may choose to do so in the future, the availability and effectiveness of any hedging transactions may be limited and we may not be able to successfully hedge our exchange rate risks. Accordingly, we may experience economic losses and negative impacts on earnings and equity as a result of foreign exchange rate fluctuations. During the second quarter and first half of 2006, the foreign currency translation adjustments to our comprehensive income were \$0.7 million and \$2.1 million, the currency transaction loss was approximately \$0.01 million and \$0.03 million, primarily as a result of the Chinese renminbi appreciating against the U.S. dollar.



**Table of Contents****Investment Risk*****Equity investments***

We have direct investments in privately held companies, which are considered in the start-up or development stages. These investments are inherently risky, as the technologies or products these companies have under development are typically in the early stages and may never materialize, and we could lose a substantial part of our investment in these companies. The Company monitors its investments for other-than-temporary impairment by considering factors including, but are not limited to, current economic and market conditions, the operating performance of the companies including current earnings trends and undiscounted cash flows and other company-specific information including recent financing rounds. The evaluation process is based on information that it requests from these privately-held companies. This information is not subject to the same disclosure regulations as U.S. publicly traded companies, and as such, the basis for these evaluations is subject to the timing and the accuracy of the data received from these companies. See also Note 5 **Equity Investments** to the Condensed Consolidated Financial Statements.

For a discussion on the investment risk of Tidetime Sun, please refer to Note 4 **Investment in Tidetime Sun** to the Condensed Consolidated Financial Statements.

**Item 4. Controls and Procedures****Disclosure Controls and Procedures**

As of the end of the period covered by this quarterly report, we carried out an evaluation, under the supervision of, and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that: (i) as of the end of the period covered by this report, our disclosure controls and procedures were effective to enable us to record, process, summarize and report information required to be included in our reports that we file or submit under the Exchange Act within the time periods required; and (ii) as of the end of the period covered by this report, our disclosure controls and procedures were effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Control over Financial Reporting**

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) during the quarter ended June 30, 2006 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION****Item 1. Legal Proceedings**

In February 2005, multiple purported securities class action complaints were filed against the Company and certain officers and directors of the Company in the United States District Court for the Southern District of New York, following the Company's announcement of anticipated financial results for the first quarter of 2005 ending on March 31, 2005. The complaints seek unspecified damages on alleged violations of federal securities laws during the period from October 26, 2004 to February 7, 2005. The complaints allege violations of the federal securities laws through the issuance of false or misleading statements during the class period covered.

On July 1, 2005, Judge Naomi Buchwald consolidated the cases under the caption *In re SINA Corporation Securities Litigation* and appointed City of Sterling Heights General Employee's Retirement System, City of St. Clair Shores Police and Fire Retirement System, and Charter Township of Clinton Police and Fire Retirement System (collectively the MAPERS Funds Group) as lead plaintiff. The MAPERS Funds Group filed an amended consolidated complaint on September 9, 2005. The Company intends to take all appropriate action in response to these lawsuits. The Company cannot estimate any possible loss at this time.

From time to time, the Company may also be subject to legal proceedings and claims in the ordinary course of business, including claims of alleged infringement of copyrights and other intellectual property rights in connection with the content published on our websites.





**Table of Contents**

**Item 1A. Risk Factors**

We have updated the risk factors previously disclosed in Part I Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2005.

***Because our operating history is limited and the revenue and income potential of our business and markets are unproven, we cannot predict whether we will meet internal or external expectations of future performance.***

We believe that our future success depends on our ability to significantly increase revenue from our operations, of which we have a limited history. Accordingly, our prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies with a limited operating history. These risks include our ability to:

offer new and innovative products;

attract buyers for our MVAS;

attract advertisers;

attract a larger audience to our network;

derive revenue from our users from fee-based Internet services;

respond effectively to competitive pressures and address the effects of strategic relationships or corporate combinations among our competitors;

maintain our current, and develop new, strategic relationships;

increase awareness of our brand and continue to build user loyalty;

attract and retain qualified management and employees;

upgrade our technology to support increased traffic and expanded services; and

expand the content and services on our network or secure certain premium content.

***Until recently, we had incurred accumulated deficits and we may incur future losses.***

We had incurred net losses through the third quarter of 2002. As of June 30, 2006 and December 31, 2005, we had retained earnings of \$43.5 million and \$26.1 million, respectively. We cannot be certain we will sustain profitability. If we do not sustain profitability, the market price of our ordinary shares may decline.

***We are relying on advertising sales as a significant part of our future revenue, but the online advertising market is subject to many uncertainties, which could cause our advertising revenues to decline.***

Our advertising revenue growth is dependent on increased revenue from the sale of advertising space on our network. The growth of online advertising in Greater China is subject to many uncertainties and many of our current and potential advertisers have limited experience with the Internet as an advertising medium, have not traditionally devoted a significant portion of their advertising expenditures or other available funds to web-based advertising, and may not find the Internet to be effective for promoting their products and services relative to traditional print and broadcast media. Our ability to generate and maintain significant advertising revenue will depend on a number of factors, many of which are beyond our control, including but not limited to:

the development and retention of a large base of users possessing demographic characteristics attractive to advertisers;

increased competition and potential downward pressure on online advertising prices and limitations on inventory;

**Table of Contents**

the development of independent and reliable means of verifying levels of online advertising and traffic; and

the effectiveness of our advertising delivery, tracking and reporting systems.

If the Internet does not become more widely accepted as a medium for advertising, our ability to generate increased revenue could be negatively affected.

Our growth in advertising revenues, to a certain extent, will also depend on our ability to increase the advertising space on our network. If we fail to increase our advertising space at a sufficient rate, our growth in advertising revenues could be hampered. Further, the increasing usage of Internet advertising blocking software may result in a decrease of our advertising revenues as the advertisers may choose not to advertise on the Internet if Internet advertising blocking software is widely used.

***We are relying on MVAS for a significant portion of our future revenue.***

MVAS revenues accounted for 42% and 49% of our total net revenues in the second quarter of 2006 and 2005, respectively. SMS revenues accounted for 72% and 69% of our MVAS revenues in the second quarter of 2006 and 2005, respectively. If users do not adopt our MVAS at a sufficient rate, or if our SMS revenues fail to grow, our revenue growth could be negatively affected. Our MVAS revenues declined significantly in 2005 from the prior year and may continue to decline in the future. Factors that may prevent us from maintaining or growing our MVAS revenues include:

our ability to develop new services that become accepted by the market;

our ability to retain existing customers of our subscription services;

our ability to attract new subscribers in a cost-effective manner;

competitors, including mobile operators, may launch competing or better products than ours;

changes in policy, process and/or system by China Mobile and/or China Unicom, on whom we rely for service delivery, billing and fee collection, and who in the past have made sudden changes that have significantly impacted our revenues and may continue to do so in the future; and

changes in government regulations, which could restrict our MVAS offering and/or our ability to market our services.

In addition to the above, we are relying on new MVAS such as MMS, IVR, CRBT, Kjava and WAP to be a significant part of our future revenue growth for MVAS. However, the current market size for these new MVAS is relatively small and adoption rates are still relatively low for these services compared to SMS services. If revenues from these services do not continue to grow significantly, our financial position, results of operations and cash flows could be materially adversely affected, the price of our ordinary shares could decline and you could lose part or all of your investment.

***With respect to MVAS, we rely on China Mobile and China Unicom for service delivery, billing and fee collection.***

Our MVAS offerings depend mainly on the cooperation arrangements with China Mobile and its subsidiaries and to a lesser extent China Unicom and its subsidiaries. We rely on China Mobile and China Unicom in the following ways: utilizing their network and gateway to provide MVAS to subscribers; utilizing their billing systems to charge the fees to our subscribers through the subscribers' mobile phone bill; utilizing their collection services to collect payments from subscribers; and relying on their infrastructure development to further develop our new products and services. As of June 30, 2006, we offered our MVAS pursuant to relationships with 31 provincial and local subsidiaries of China Mobile and 22 provincial subsidiaries of China Unicom. If either China Mobile or China Unicom chooses not to continue the cooperation arrangements with us, our MVAS revenues and operating profitability could be materially and negatively affected.

China Mobile and China Unicom may choose to increase the fees charged for providing their services in the future, and if they choose to increase such fees, our gross margin for MVAS and our operating profitability may be negatively impacted. Based on the arrangements with China Mobile and its subsidiaries, China Mobile generally retains 15% of the fees for content value-added services we provide to our users via their platform for fee collection. In addition, China Mobile deducts transmission fees from our portion of

**Table of Contents**

the service fees. The amount of such transmission fee is charged on a per message basis and varies for different products and message volume. For the second quarter of 2006 and 2005, we received on average 74% and 76%, respectively, of the amount we charged to our users from the China Mobile platform after China Mobile deducted the fees for collection and transmission. Based on the arrangements with China Unicom and its subsidiaries, China Unicom typically retains 20% of the fees for content value-added services we provide to our users via their platform if they charge us for transmission cost or between 21% and 29% if they do not charge us for transmission cost. For the second quarter of 2006 and 2005, we received on average 63% and 68%, respectively, of the amount we charged to our users from the China Unicom platform after China Unicom deducted the fees for collection and transmission.

In the past, mobile operators have made sudden and unexpected changes in their policies, processes and systems, which have harmed our business. For example:

In mid 2004, mobile operators began transitioning SMS to new billing platforms, which has resulted in added operational controls and procedures in areas such as customer subscription and customer billing. Such change has increased the difficulties for new user recruitment and the failure rate for fee collection from our SMS users.

In January 2005, China Mobile stopped its MMS Album service, which allowed users to retrieve their subscribed MMS messages from China Mobile's website when the subscribed MMS messages could not be successfully delivered to their mobile phones. With the termination of MMS Album, we are no longer able to collect fees from users when the MMS messages could not be delivered to such users' mobile phones.

In March 2005, China Mobile began migrating MMS onto a new billing platform, which has resulted in added operational controls and procedures and, correspondingly, increased difficulties for new user recruitment and increased the failure rate for fee collection from our users.

In April 2006, China Unicom issued a new policy that sets price ceilings for usage-based and monthly subscription SMS. Such change may require us to lower our current prices on certain SMS or discontinue offering these services completely.

In July 2006, China Mobile made significant changes to their policy on subscription-based MVAS, which included extending the trial period and requiring double reminders on new MVAS subscriptions as well as sending SMS reminders to existing monthly subscribers of SMS, MMS and WAP to inform them of their MVAS subscription and fee information. Certain provincial subsidiaries, such as Guangdong Mobile, one of China Mobile's largest provincial subsidiaries, have begun to discontinue charging MVAS users monthly subscription fees unless the users reply to the SMS reminders and reconfirm their subscription. Other provincial subsidiaries are expected to announce additional measures of their own. In addition, it is expected that China Mobile's provincial subsidiaries will begin canceling existing WAP subscriptions that have been inactive for the prior four months and existing SMS subscriptions of users who have not successfully received more than three SMS messages during the month. These policy changes from China Mobile could significantly reduce the Company's ability to acquire new monthly MVAS subscribers and significantly increase the churn rate of existing monthly MVAS subscribers. Other Chinese mobile operators, such as China Unicom, may also announce similar measures.

Our mobile operators could make further changes at any time, including requiring service providers (SPs) to use the mobile operators' customer service and/or marketing service and charging for these services; implementing new billing rules, such as reducing MVAS fees that can be charged to users, disallowing SPs to bill certain inactive users and limiting the amount of MVAS fees that can be billed; issuing new rules on how WAP SPs are placed on their browsers, which significantly determines WAP revenues; and limiting the product offerings of SPs by working directly with content providers to launch competing services or giving exclusive rights to certain SPs to offer certain MVAS. Any change in policy, process or system by the mobile operators could result in a material reduction of our MVAS revenues.

If China Mobile or China Unicom restricts or disallows some or all MVAS to be charged on a monthly subscription basis, our revenues from MVAS could be severely impacted. We currently charge our users who have

registered to be billed on a monthly basis even if they do not use the service in a particular month. If China Mobile or China Unicom does not allow us to charge monthly fees for users who do not use our service in a particular month, our MVAS revenues could be negatively impacted. For the second quarter of 2006, approximately 78% of our MVAS revenues were derived from monthly subscription products, which mainly consist of SMS, MMS and WAP.

In the past, China Mobile and China Unicom have imposed penalties on MVAS providers for violating certain operating policies relating to MVAS. In some cases, they stopped making payments to certain service providers for severe violations. To date, the

**Table of Contents**

penalties we have received have been insignificant in dollar amounts and have been accrued for, but it is difficult to determine the specific conduct that might be interpreted as violating such operating policies. In the future, if China Mobile or China Unicom imposes more severe penalties on us for policy violations, our revenues from MVAS may be negatively impacted for the period when such penalties are imposed.

We are subject to potential liability and penalty for delivering inappropriate content through our MVAS. One of the violations cited in the notice for temporary termination of our IVR service at the end of July 2004 was that we had provided inappropriate content to our mobile subscribers through our IVR service. The definition and interpretation of inappropriate content in many cases are vague and subjective. We are not sure whether mobile operators including China Mobile and China Unicom or the Chinese government will find our other mobile content inappropriate and therefore prevent us from operating the MVAS relating to such content in the future. If they prevent us from offering such services, our revenues from MVAS will suffer significantly.

If China Mobile's or China Unicom's systems encounter technical problems, or if they refuse to cooperate with us, our MVAS offerings may cease or be severely disrupted, which could have a significant and adverse impact on our operating results.

A portion of our MVAS revenues is currently estimated based on our internal records of billings and transmissions for the month, adjusted for prior period confirmation rates from mobile operators and prior period discrepancies between internal estimates and confirmed amounts from mobile operators. Historically, there have been no significant true up adjustments to our estimates. If there was no consistent confirmation rates trend or if there were continuous significant true up adjustments to our estimates under the new billing platforms, we will need to rely on the billing statements from the mobile operators to record revenues. Due to the time lag of receiving the billing statements, our MVAS revenues may fluctuate with the collection of billing statements if we were to record the MVAS revenues when we receive the billing statements. For the second quarter of 2006, approximately 24% of our MVAS revenues were estimated at period end.

***The markets for MVAS and Internet services are highly competitive, and we may be unable to compete successfully against new entrants and established industry competitors, some of which have greater financial resources than we do or currently enjoy a superior market position than we do.***

There is significant competition among MVAS providers. A large number of independent MVAS providers compete against us. We may be unable to continue to grow our revenues from these services in this competitive environment. In addition, the major mobile operators in China, China Mobile and China Unicom, may potentially enter the business of content development. Any of our present or future competitors may offer MVAS which provide significant technology, performance, price, creativity or other advantages, over those offered by us, and therefore achieve greater market acceptance than ours.

The Chinese market for Internet content and services is competitive and rapidly changing. Barriers to entry are relatively low, and current and new competitors can launch new websites or services at a relatively low cost. Many companies offer Chinese language content and services, including informational and community features, fee-based services and email and electronic commerce services in the Greater China market that may be competitive with our offerings. In addition, providers of Chinese language Internet tools and services may be acquired by, receive investments from or enter into other commercial relationships with large, well-established and well-financed Internet, media or other companies. We also face competition from providers of software and other Internet products and services that incorporate search and retrieval features into their offerings. In addition, entities that sponsor or maintain high-traffic websites or provide an initial point of entry for Internet users, such as ISPs, including large, well-capitalized entities such as Microsoft (MSN), Yahoo! Inc., eBay Inc., Google Inc. ( Google ) and America Online Inc, currently offer and could further develop or acquire content and services that compete with those that we offer. Companies such as these may have greater financial resources and assets, better brand recognition, more developed sales and other internal organizations, more customers and more extensive operating histories. As a result, such companies may be able to quickly provide competitive services and obtain a significant number of customers. We expect that as Internet usage in Greater China increases and the Greater China market becomes more attractive to advertisers and for conducting electronic commerce, large global competitors may increasingly focus their resources on the Greater China market. We also compete for advertisers with traditional media companies, such as newspapers,

television networks and radio stations that have a longer history of use and greater acceptance among advertisers.

In the areas of online games, search, instant messaging and user-generated content such as blogs, our other areas of focus for future business growth, there is intense competition from domestic and international companies. These include domestic companies each focusing on one sector and large, international companies that intend to extend their businesses in the China market. The online gaming industry, for example, is dominated by domestic online game operators such as Shanda, Netease and The9. The main competitors for search are Baidu, Yahoo!/Alibaba and Google, the competitors for our instant messaging service are Tencent's QQ



**Table of Contents**

and Microsoft's MSN Messenger, and the competitors for our user-generated content such as blogs are BlogCN, Bokee.com, ChinaBlog and Baidu KongJian. Many of our competitors have a longer history of providing these online services and currently offer a greater breadth of products which may be more popular than our online offerings. Many of these companies are focused solely on one area of our business and are able to devote all of their resources to that business area and to more quickly adapt to changing technology or market conditions. These companies may therefore have a competitive advantage over us with respect to these business areas. A number of our current and potential future competitors have greater financial and other resources than we have, and may be able to more quickly react to changing consumer requirements and demands, deliver competitive services at lower prices and more effectively respond to new Internet technologies or technical standards.

Increased competition could result in reduced page views, loss of market share and revenues, and lower profit margins from reduced pricing for Internet-based services.

***Our investment in online games, search, instant messaging and services related to user-generated content may not be successful.***

Online games, search, instant messaging and user-generated content such as blogs are currently some of the fastest growing online services in the PRC. We have invested and intend to expand in these areas. For example, we have developed our own search engine, we have acquired Davidhill Capital Inc. ( Davidhill ) and its instant messaging platform, and we have recently added SINA blog, which offers users a range of blog services. Some of our competitors have entered these markets ahead of us and have achieved significant market positions. Our main competitors in online games, search, instant messaging and user-generated content include Shanda, Netease, The9, Baidu, Yahoo!/Alibaba, Tencent's QQ, MSN Messenger, BlogCN, Bokee.com, ChinaBlog and Baidu KongJian. Our competitors in these areas tend to be more specialized in these specific markets and may have access to greater resources, which may give them a competitive advantage over us. We cannot assure you that we will succeed in these markets despite our investments of time and funds to address these markets. If we fail to achieve a significant position in these markets, we will fail to realize our intended returns in these investments. Moreover, our competitors who succeed may enjoy increased revenues and profits from an increase in market share in any of these specific markets, and our results and share price could suffer as a result.

***We may not be able to manage our expanding operations effectively, which could harm our business.***

We have expanded rapidly by acquiring companies and entering into joint ventures. These new businesses and joint ventures provide various services such as MVAS, instant messaging and online games. We anticipate continuous expansion in our business, both through further acquisitions and internal growth, as we address growth in our customer base and market opportunities. In addition, the geographic dispersion of our operations as a result of acquisitions and overall internal growth requires significant management resources that our locally-based competitors do not need to devote to their operations. In order to manage the expected growth of our operations and personnel, we will be required to improve and implement operational and financial systems, procedures and controls, and expand, train and manage our growing employee base. Further, our management will be required to maintain and expand our relationships with various other websites, Internet and other online service providers and other third parties necessary to our business. We cannot assure you that our current and planned personnel, systems, procedures and controls will be adequate to support our future operations. If we are not successful in establishing, maintaining and managing our personnel, systems, procedures and controls, our business will be materially and adversely affected.

***If we fail to successfully develop and introduce new products and services, our competitive position and ability to generate revenues could be harmed.***

We are developing new products and services. The planned timing or introduction of new products and services is subject to risks and uncertainties. Actual timing may differ materially from original plans. Unexpected technical, operational, distribution or other problems could delay or prevent the introduction of one or more of our new products or services. Moreover, we cannot be sure that any of our new products and services will achieve widespread market acceptance or generate incremental revenue. If our efforts to develop, market and sell new products and services to the market are not successful, our financial position, results of operations and cash flows could be materially adversely affected, the price of our ordinary shares could decline and you could lose part or all of your investment.

***If we are unable to keep up with the rapid technological changes of the Internet industry, our business may suffer.***

The Internet industry is experiencing rapid technological changes. For example, with the advances of search engines, Internet users may choose to access information through search engines instead of web portals. With the advent of Web 2.0, the interests and

**Table of Contents**

preferences of Internet users may shift to user-generated content, such as blogs. As broadband becomes more accessible, Internet users may demand contents in audio- and video-rich format. With the development of 2.5G and soon 3G in China, mobile users may shift from the current predominant text messaging services to newer applications, such as multi-media messaging services, wireless e-commerce, music and video downloads and mobile games. Our future success will depend on our ability to anticipate, adapt and support new technologies and industry standards. If we fail to anticipate and adapt to these and other technological changes, our market share and our profitability could suffer.

***Our strategy of acquiring complementary assets, technologies and businesses and entering into joint ventures may fail and may result in equity or earnings dilution.***

As part of our business strategy, we have acquired and intend to continue to identify and acquire assets, technologies and businesses that are complementary to our existing business. In January 2003 we acquired Memestar Limited, an MVAS company, in March 2004 we acquired Crillion Corp., an MVAS company, and in October 2004, we acquired Davidhill, an instant messaging technology platform. Acquired businesses or assets may not yield the results we expected. In addition, acquisitions could result in the use of substantial amounts of cash, potentially dilutive issuances of equity securities, significant amortization expenses related to goodwill and other intangible assets and exposure to potential unknown liabilities of the acquired business. Moreover, the costs of identifying and consummating acquisitions, and integrating the acquired businesses into ours, may be significant, and the integration of acquired business may be disruptive to our business operations. In addition, we may have to obtain approval from the relevant PRC governmental authorities for the acquisitions and have to comply with any applicable PRC rules and regulations, which may be costly. In the event our acquisitions are not successful, our financial conditions and results of operation may be materially adversely affected.

***Our business and growth could suffer if we are unable to hire and retain key personnel that are in high demand.***

We depend upon the continued contributions of our senior management and other key personnel, many of whom are difficult to replace. The loss of the services of any of our executive officers or other key employees could harm our business. We have experienced recent changes to our executive management team. Our future success will also depend on our ability to attract and retain highly skilled technical, managerial, editorial, marketing, sales and customer service personnel, especially qualified personnel for our international operations in Greater China. Qualified individuals are in high demand, and we may not be able to successfully attract, assimilate or retain the personnel we need to succeed.

***We may be adversely affected by complexity, uncertainties and changes in PRC regulation of Internet business and companies, including limitations on our ability to own key assets such as our website.***

The Chinese government heavily regulates its Internet sector, including the legality of foreign investment in the Chinese Internet sector, the existence and enforcement of content restrictions on the Internet and the licensing and permit requirements for companies in the Internet industry. Because these laws, regulations and legal requirements with regard to the Internet are relatively new and evolving, their interpretation and enforcement involve significant uncertainty. In addition, the Chinese legal system is a civil law system in which decided legal cases may be cited for reference but have little precedential value. As a result, in many cases it is difficult to determine what actions or omissions may result in liability. Issues, risks and uncertainties relating to China's government regulation of the Chinese Internet sector include the following:

We only have contractual control over our website in China; we do not own it due to the restriction of foreign investment in businesses providing value-added telecommunication services, including computer information services, MVAS or electronic mail box services.

In addition, uncertainties relating to the regulation of the Internet business in China, including evolving licensing practices, give rise to the risk that permits, licenses or operations at some of our companies may be subject to challenge, which may be disruptive to our business, or subject us to sanctions, requirements to increase capital or other conditions or enforcement, or compromise enforceability of related contractual arrangements, or have other harmful effects on us.

On December 11, 2001, the day China formally joined the World Trade Organization, the PRC State Council promulgated the FITE Regulations, which became effective on January 1, 2002. The FITE Regulations stipulate that the foreign party to a foreign-invested telecommunications enterprise can hold an equity share in such foreign-invested telecommunications enterprise that provides basic telecommunication services or value-added telecommunication services, ultimately not to exceed 49% or 50%, respectively. The Administrative Measures for Telecommunications Business Operating License were promulgated by MII on December 26, 2001 and came into effect on January 14, 2002 to supplement the FITE Regulations.

**Table of Contents**

However, there are still uncertainties regarding the interpretation and application of the FITE Regulations.

The numerous and often vague restrictions on acceptable content in China subject us to potential civil and criminal liability, temporary blockage of our website or complete cessation of our website. For example, the State Secrecy Bureau, which is directly responsible for the protection of state secrets of all Chinese government and Chinese Communist Party organizations, is authorized to block any website it deems to be leaking state secrets or failing to meet the relevant regulations relating to the protection of state secrets in the distribution of online information.

Because the definition and interpretation of prohibited content are in many cases vague and subjective, it is not always possible to determine or predict what and how content might be prohibited under existing restrictions or restrictions that might be imposed in the future. For example, in January 2005, the Chinese State Administration of Radio, Film & Television ( SARFT ), which regulates radio and television stations in China, issued a notice prohibiting commercials for MVAS related to fortune-telling from airing on radio and television stations, effective in February 2005. This notice could also lead to further actions by other Chinese government authorities to prohibit the sale of such fortune-telling related SMS, which could have a material adverse effect on our financial position, results of operations, or cash flows. SARFT or other Chinese government authorities may prohibit the marketing of other MVAS via a channel we depend on to generate revenues, which could also have a material adverse effect on our financial position, results of operations or cash flows.

Certain Chinese governmental authorities have stated publicly that they are in the process of preparing new laws and regulations that will govern Internet activities. The areas of regulation currently include online advertising, online news reporting, online publishing, and the provision of industry-specific (e.g., drug-related) information over the Internet. Other aspects of our online operations may be subject to regulation in the future. Our operations may not be consistent with these new regulations when they are put into effect and, as a result, we could be subject to severe penalties as discussed above.

The governing body of China's mobile industry, from time to time issues policies that regulate the business practices relating to MVAS. We cannot predict the timing or substance of such regulations. Such regulations may have a negative impact on our business.

In July 2006, MII issued a Notice on Strengthening Management of Foreign Investment in and Operation of Value-added Telecommunication Services Business. The Notice, among other things, provides that foreign investors who intend to invest in and operate value-added telecommunication services in China shall strictly abide by applicable rules in applying for the establishment of foreign invested telecommunication enterprises and applying for relevant licenses for operating a value-added telecommunication services business. In addition, the Notice states that domestic telecommunication companies shall not by any means lease, lend, transfer or sell their telecommunication service operation license to any foreign investor and shall not in any manner provide resources, premises, facilities, equipment or other features to any foreign investor that operates a telecommunication service business illegally in China. The Notice sets forth certain requirements for domestic value-added telecommunication companies. An operator of value-added telecommunication services must itself own the domain names and trademarks used by such operator. In addition, an operator of value-added telecommunication services shall have the necessary premises, facilities and equipment and shall improve measures to protect the security of network and information, establish relevant management structure to protect the safety of information, set up emergency procedures to protect the security of network and information and be responsible for the safety of information, all in accordance with applicable regulations. Domestic companies which have already obtained value-added telecommunication services licenses must evaluate their compliance with these requirements, take corrective action in accordance with these requirements and submit results of such examination and self-correction to the MII before November 1, 2006. Companies which do not comply with these requirements must rectify their non-compliance within a specified time period or may have their value-added telecommunication service operation licenses revoked.

We conduct all of our Internet information services, advertising and MVAS in China via certain significant domestic Variable Interest Entities, or VIEs. We are in the process of evaluating our compliance (including the compliance of our VIEs) with these requirements. We anticipate that we may need to modify certain aspects of our business and corporate structure in order to comply with these requirements.

**Table of Contents**

The interpretation and application of existing Chinese laws, regulations and policies, the stated positions of the MII and possible new laws, regulations or policies have created substantial uncertainties regarding the legality of existing and future foreign investments in, and the businesses and activities of, Internet businesses in China, including our business.

***In order to comply with PRC regulatory requirements, we operate our main businesses through companies with which we have contractual relationships but in which we do not have controlling ownership. If the PRC government determines that our agreements with these companies are not in compliance with applicable regulations, our business in the PRC could be adversely affected.***

The Chinese government restricts foreign investment in Internet-related, MVAS and advertising businesses, including Internet access, distribution of content over the Internet and MVAS, and advertising via the Internet. Accordingly, we operate our Internet-related and MVAS businesses in China through several variable interest entities, or VIEs, that are owned principally or completely by certain of our PRC employees or PRC employees of our subsidiaries. We control these companies and operate these businesses through contractual arrangements with the respective companies and their individual owners, but we have no equity control over these companies. Such restrictions and arrangements are prevalent in other PRC companies we have acquired.

As discussed in the risk factor above titled "We may be adversely affected by complexity, uncertainties and changes in PRC regulation of Internet business and companies, including limitations on our ability to own key assets such as our website", in July 2006, the MII issued a "Notice on Strengthening Management of Foreign Investment in and Operation of Value-added Telecommunication Services Business." The Notice sets forth certain restrictions applicable to foreign investors who intend to invest in and operate value-added telecommunication services in China and to domestic value-added telecommunication companies. We are in the process of evaluating our compliance (including the compliance of our VIEs) with these requirements. We anticipate that we may need to modify certain aspects of our business and corporate structure in order to comply with these requirements.

We cannot be sure that the PRC government would view our operating arrangements to be in compliance with PRC licensing, registration or other regulatory requirements (including without limitation the requirements described in the Notice issued by MII in July 2006), with existing policies or with requirements or policies that may be adopted in the future. If we are determined not to be in compliance, the PRC government could revoke our business and operating licenses, require us to discontinue or restrict our operations, restrict our right to collect revenues, block our website, require us to restructure our business, corporate structure or operations, impose additional conditions or requirements with which we may not be able to comply, impose restrictions on our business operations or on our customers, or take other regulatory or enforcement actions against us that could be harmful to our business. We may also encounter difficulties in obtaining performance under or enforcement of related contracts.

***We rely on contractual arrangements with our VIEs for our China operations, which may not be as effective in providing control over these entities as direct ownership.***

Because PRC regulations restrict our ability to provide Internet content, MVAS and advertising services directly in China, we are dependent on our VIEs in which we have little or no equity ownership interest and must rely on contractual arrangements to control and operate these businesses. These contractual arrangements may not be as effective in providing control over these entities as direct ownership. For example, the VIEs could fail to take actions required for our business or fail to maintain our China websites despite their contractual obligation to do so. These companies are able to transact business with parties not affiliated with us. If these companies fail to perform under their agreements with us, we may have to rely on legal remedies under Chinese law, which we cannot be sure would be effective. In addition, we cannot be certain that the individual equity owners of the VIEs would always act in the best interests of SINA, especially if they leave SINA.

Substantially all profits generated from our VIEs are paid to the subsidiaries of ours in China through related party transactions under contractual agreements. We believe that the terms of these contractual agreements are in compliance with the laws in China. The tax authorities in China have examined some of these contractual agreements in the past and have not raised any comment. However, due to the uncertainties surrounding the interpretation of the transfer pricing rules relating to related party transactions in China, it is possible that in the future tax authorities in China may challenge the transfer prices that we have used for related party transactions among our entities in China.

In the event the tax authorities challenge our VIE structure, we may be forced to restructure our business operation, which could have a material adverse effect on our business.



**Table of Contents**

***If tax benefits currently available to us in China were no longer available, our effective income tax rates for our China operations could increase to 33%.***

We are incorporated in the Cayman Islands where no income taxes are imposed. We have operations in four tax jurisdictions including China, the U.S., Hong Kong and Taiwan. For the U.S., Hong Kong and Taiwan, we have incurred net accumulated operating losses for income tax purposes. We believe that it is more likely than not that these net accumulated operating losses will not be utilized in the future and hence we have not recorded income tax provisions or benefits for these locations. We do not expect that we will record any income tax provisions for our operations in the U.S., Hong Kong and Taiwan in the foreseeable future.

We generated substantially all our net income from our China operations. Our China operations are conducted through various subsidiaries and VIEs. Pursuant to the PRC Income Tax Laws, our subsidiaries and VIEs are generally subject to Enterprise Income Taxes ( EIT ) at a statutory rate of 33%, consisting of a 30% national income tax and a 3% local income tax. However, some of our subsidiaries and VIEs are qualified new technology enterprises, and under PRC Income Tax Laws, they are subject to a preferential tax rate of 15%. In addition, some of our subsidiaries are Foreign Investment Enterprises, and under PRC Income Tax Laws, they are entitled to either a three-year tax exemption followed by three years with a 50% reduction in the tax rate, commencing the first operating year, or a two-year tax exemption followed by three years with a 50% reduction in the tax rate, commencing the first profitable year. To the extent that our VIEs have undistributed after tax net income, we have to pay dividend tax on behalf of the employees when we try to distribute the dividend from these local entities in the future. The dividend tax rate is 20%. Based on our current operating structure and preferential tax treatments available to us in China, we expect our effective income tax rates to be between 5% to 10% for fiscal year 2006. Such expected effective rates are subject to change at any time if Chinese tax authorities challenge us on our current tax arrangements between our subsidiaries and VIEs. Over the longer term, if the Chinese government phases out preferential tax treatment for foreign investment enterprises or for new technology enterprises, our effective tax rates for the PRC operation can be increased to as high as 33%.

Due to our operating and tax structures in the PRC, we have entered into technical and other service agreements between our subsidiaries and our VIEs in the PRC, pursuant to which our subsidiaries provide technical and other services to our VIEs in exchange for substantially all net income of these VIEs. We incur a 5% business tax when our subsidiaries receive the fees from the VIEs, which we include in our operating expenses as the cost of transferring economic benefit generated from these VIEs. We believe that the terms of such service agreements are in compliance with the laws of the PRC. Some of these agreements were reviewed by the tax authorities in the PRC in the past and no comments were made. However, due to the uncertainties surrounding the interpretation of the tax transfer pricing rules relating to related party transactions in the PRC, it is possible that in the future tax authorities in the PRC might challenge the transfer prices that we used for the related party transactions among our entities in the PRC.

***Restrictions on paying dividends or making other payments to us bind our subsidiaries and VIEs in China.***

We are a holding company and do not have any assets or conduct any business operations in China other than our investments in our subsidiaries in China, including SINA.com Technology (China) Co., Ltd., Star-Village.com (Beijing) Internet Technology Ltd., Beijing New Media Information Technology Co. Ltd., Beijing SINA Internet Technology Service Co. Ltd., Beijing SINA Information Technology Co. Ltd. and others; and our VIEs. As a result, we depend on dividend payments from our subsidiaries in China for our revenues after they receive payments from our VIEs in China under various services and other arrangements. We cannot make any assurance that our subsidiaries in China can continue to receive the payments as arranged under our contracts with those VIEs. To the extent that these VIEs have undistributed after tax net income, we have to pay tax on behalf of the employees when we try to distribute the dividend from these local entities in the future. The dividend tax rate is 20%. In addition, under Chinese law, our subsidiaries are only allowed to pay dividends to us out of their accumulated profits, if any, as determined in accordance with Chinese accounting standards and regulations. Moreover, our Chinese subsidiaries are required to set aside at least 10% of their respective accumulated profits, if any, and up to 50% of their registered capital to fund certain mandated reserve funds that are not payable or distributable as cash dividends.

The Chinese government also imposes controls on the convertibility of renminbi into foreign currencies and, in certain cases, the remittance of currency out of China. We may experience difficulties in completing the

administrative procedures necessary to obtain and remit foreign currency. See *Currency fluctuations and restrictions on currency exchange may adversely affect our business, including limiting our ability to convert Chinese renminbi into foreign currencies and, if renminbi were to decline in value, reducing our revenues in U.S. dollar terms.* If we or any of our subsidiaries are unable to receive all of the revenues from our operations through these contractual or dividend arrangements, we may be unable to effectively finance our operations or pay dividends on our ordinary shares.

**Table of Contents**

***Even if we are in compliance with Chinese governmental regulations relating to licensing and foreign investment prohibitions, the Chinese government may prevent us from advertising or distributing content that it believes is inappropriate and we may be liable for such content or we may have to stop profiting from such content.***

China has enacted regulations governing Internet access and the distribution of news and other information. In the past, the Chinese government has stopped the distribution of information over the Internet or through MVAS that it believes to violate Chinese law, including content that it believes is obscene, incites violence, endangers national security, is contrary to the national interest or is defamatory. In addition, we may not publish certain news items, such as news relating to national security, without permission from the Chinese government. Furthermore, the Ministry of Public Security has the authority to cause any local Internet service provider to block any website maintained outside China at its sole discretion. Even if we comply with Chinese governmental regulations relating to licensing and foreign investment prohibitions, if the Chinese government were to take any action to limit or prohibit the distribution of information through our network or via our MVAS, or to limit or regulate any current or future content or services available to users on our network, our business could be significantly harmed.

Because the definition and interpretation of prohibited content is in many cases vague and subjective, it is not always possible to determine or predict what and how content might be prohibited under existing restrictions or restrictions that might be imposed in the future. At the end of July 2004, our IVR service was temporarily terminated by China Mobile for violating certain operating procedures. One of the violations cited in the notice for temporary termination was that we had provided inappropriate content to our mobile subscribers through our IVR service. We are not sure whether mobile operators including China Mobile and China Unicom or the Chinese government will find our other mobile content inappropriate and therefore prevent us from operating the MVAS relating to such content in the future. If they prevent us from offering such services, our profit from MVAS will suffer.

In January 2005, the Chinese State Administration of Radio, Film and Television ( SARFT ), which regulates radio and television stations in China, issued a notice prohibiting commercials for MVAS related to fortune-telling from airing on radio and television stations effective in February 2005. This notice could also lead to further actions by other Chinese government authorities to prohibit the sale of such fortune-telling related SMS which could have a material adverse effect on our financial position, results of operations, or cash flows. SARFT or other Chinese government authorities may prohibit the marketing of other MVAS via a channel we depend on to generate revenues, which could have a material adverse effect on our financial position, results of operations or cash flows.

We are also subject to potential liability for content on our websites that is deemed inappropriate and for any unlawful actions of our subscribers and other users of our systems. Furthermore, we are required to delete content that clearly violates the laws of China and report content that we suspect may violate Chinese law. It is difficult to determine the type of content that may result in liability for us, and if we are wrong, we may be prevented from operating our websites.

***The law of the Internet remains largely unsettled, which subjects our business to legal uncertainties that could harm our business.***

Due to the increasing popularity and use of the Internet and other online services, it is possible that a number of laws and regulations may be adopted with respect to the Internet or other online services covering issues such as user privacy, pricing, content, copyrights, distribution, antitrust and characteristics and quality of products and services. Furthermore, the growth and development of the market for electronic commerce may prompt calls for more stringent consumer protection laws that may impose additional burdens on companies conducting business online. The adoption of any additional laws or regulations may decrease the growth of the Internet or other online services, which could, in turn, decrease the demand for our products and services and increase our cost of doing business.

Moreover, the applicability to the Internet and other online services of existing laws in various jurisdictions governing issues such as property ownership, sales and other taxes, libel and personal privacy is uncertain and may take years to resolve. For example, new tax regulations may subject us or our customers to additional sales and income taxes. Any new legislation or regulation, the application of laws and regulations from jurisdictions whose laws do not currently apply to our business, or the application of existing laws and regulations to the Internet and other online services could significantly disrupt our operations.

***The Chinese legal system has inherent uncertainties that could limit the legal protections available to you.***

Our contractual arrangements with our variable interest entities in China are governed by the laws of the People's Republic of China. China's legal system is based upon written statutes. Prior court decisions may be cited for reference but are not binding on subsequent cases and have limited value as precedents. Since 1979, the Chinese legislative bodies have promulgated laws and

**Table of Contents**

regulations dealing with economic matters such as foreign investment, corporate organization and governance, commerce, taxation and trade. However, because these laws and regulations are relatively new, and because of the limited volume of published decisions and their non-binding nature, the interpretation and enforcement of these laws and regulations involve uncertainties, and therefore you may not have legal protections for certain matters in China.

***You may experience difficulties in effecting service of legal process, enforcing foreign judgments or bringing original actions in China based on United States or other foreign laws against us.***

We conduct our operations in China and a significant portion of our assets is located in China. In addition, some of our directors and executive officers reside within China, and substantially all of the assets of these persons are located within China. As a result, it may not be possible to effect service of process within the United States or elsewhere outside China upon those directors or executive officers, including with respect to matters arising under U.S. federal securities laws or applicable state securities laws. Moreover, our Chinese counsel has advised us that China does not have treaties with the U.S. and many other countries that provide for the reciprocal recognition and enforcement of judgment of courts. As a result, recognition and enforcement in China of judgments of a court of the U.S. or any other jurisdiction in relation to any matter may be difficult or impossible.

***We may have to register our encryption software with Chinese regulatory authorities, and if they request that we change our encryption software, our business operations could be disrupted as we develop or license replacement software.***

Pursuant to the *Regulations for the Administration of Commercial Encryption* promulgated at the end of 1999, foreign and domestic Chinese companies operating in China are required to register and disclose to Chinese regulatory authorities the commercial encryption products they use. Because these regulations do not specify what constitutes encryption products, we are unsure as to whether or how they apply to us and the encryption software we utilize. We may be required to register, or apply for permits with the relevant Chinese regulatory authorities for, our current or future encryption software. If Chinese regulatory authorities request that we change our encryption software, we may have to develop or license replacement software, which could disrupt our business operations.

***Privacy concerns may prevent us from selling demographically targeted advertising in the future and make us less attractive to advertisers.***

We collect personal data from our user base in order to better understand our users and their needs and to help our advertisers target specific demographic groups. If privacy concerns or regulatory restrictions prevent us from selling demographically targeted advertising, we may become less attractive to advertisers. For example, as part of our future advertisement delivery system, we may integrate user information such as advertisement response rate, name, address, age or email address, with third-party databases to generate comprehensive demographic profiles for individual users. In Hong Kong, however, we would be in violation of the *Hong Kong Personal Data Ordinance* unless individual users expressly consented to this integration of their personal information. The ordinance provides that an Internet company may not collect information on its users, analyze the information for a profile of the user's interests and sell or transmit the profiles to third parties for direct marketing purposes without the user's consent. If we are unable to construct demographic profiles for Internet users because they refuse to give consent, we will be less attractive to advertisers and our business could suffer.

***Concerns about the security of electronic commerce transactions and confidentiality of information on the Internet may reduce use of our network and impede our growth.***

A significant barrier to electronic commerce and communications over the Internet in general has been a public concern over security and privacy, especially the transmission of confidential information. If these concerns are not adequately addressed, they may inhibit the growth of the Internet and other online services generally, especially as a means of conducting commercial transactions. If a well-publicized Internet breach of security were to occur, general Internet usage could decline, which could reduce traffic to our destination sites and impede our growth.

***We may not be able to adequately protect our intellectual property, which could cause us to be less competitive.***

We rely on a combination of copyright, trademark and trade secret laws and restrictions on disclosure to protect our intellectual property rights. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain and use our technology. Monitoring unauthorized use of our products is difficult and costly, and we cannot be certain that the steps we have taken will prevent misappropriations of our technology,

particularly in foreign countries where the laws may not protect our

**Table of Contents**

proprietary rights as fully as in the United States. From time to time, we may have to resort to litigation to enforce our intellectual property rights, which could result in substantial costs and diversion of our resources.

***We may be exposed to infringement claims by third parties, which, if successful, could cause us to pay significant damage awards.***

Third parties may initiate litigation against us alleging infringement of their proprietary rights. In the event of a successful claim of infringement and our failure or inability to develop non-infringing technology or license the infringed or similar technology on a timely basis, our business could be harmed. In addition, even if we are able to license the infringed or similar technology, license fees could be substantial and may adversely affect our results of operations.

***We may be subject to claims based on the content we provide over our network and the products and services sold on our network, which, if successful, could cause us to pay significant damage awards.***

As a publisher and distributor of content and a provider of services over the Internet, we face potential liability for defamation, negligence, copyright, patent or trademark infringement and other claims based on the nature and content of the materials that we publish or distribute; the selection of listings that are accessible through our branded products and media properties, or through content and materials that may be posted by users in our classifieds, message board and chat room services; losses incurred in reliance on any erroneous information published by us, such as stock quotes, analyst estimates or other trading information; unsolicited email, lost or misdirected messages, illegal or fraudulent use of email or interruptions or delays in email service; and product liability, warranty and similar claims to be asserted against us by end users who purchase goods and services through our SinaMall and any future electronic commerce services we may offer.

We may incur significant costs in investigating and defending any potential claims, even if they do not result in liability. Although we carry general liability insurance, our insurance may not cover potential claims of this type and may not be adequate to indemnify us against all potential liabilities.

***We have contracted with third parties to provide content and services for our portal network and we may lose users and revenue if these arrangements are terminated.***

We have arrangements with a number of third parties to provide content and services to our websites. In the area of content, we have relied and will continue to rely almost exclusively on third parties for content that we publish under the SINA brand. Although no single third party content provider is critical to our operations, if these parties fail to develop and maintain high-quality and successful media properties, or if a large number of our existing relationships are terminated, we could lose users and advertisers and our brand could be harmed. We have recently experienced fee increases from some of our content providers. If this trend continues, our gross profit from online advertising may be adversely affected. In addition, the Chinese government has the ability to restrict or prevent state-owned media from cooperating with us in providing certain content to us, which will result in a significant decrease of the amount of content we can publish on our website. We may lose users if the Chinese government chooses to restrict or prevent state-owned media from cooperating with us, in which case our revenues will be impacted negatively.

In the area of web-based services, we have contracted with third party content providers for integrated web search technology to complement our directory and navigational guide, and with various third-party providers for our principal Internet connections. If we experience significant interruptions or delays in service, or if these agreements terminate or expire, we may incur additional costs to develop or secure replacement services and our relationship with our users could be harmed.

A substantial part of our non-advertising revenues is generated through MVAS where we depend on mobile network operators for services delivery and payment collection. If we were unable to continue these arrangements, our MVAS could be severely disrupted or discontinued. Furthermore, we are highly dependent on these mobile service providers for our profitability in that they can choose to increase their service fees at will.

We depend on a third party's proprietary and licensed advertising serving technology to deliver advertisements to our network. If the third party fails to continue to support its technology or if its services fail to meet the advertising needs of our customers and we cannot find an alternative solution on a timely basis, our advertising revenues could decline.

*Underdeveloped telecommunications infrastructure has limited, and may continue to limit, the growth of the Internet market in China which, in turn, could limit our ability to grow our business.*



**Table of Contents**

The telecommunications infrastructure in China is not well developed. Although private sector ISPs exist in China, almost all access to the Internet is accomplished through ChinaNet, China's primary commercial network, which is owned and operated by China Telecom and China Netcom under the administrative control and regulatory supervision of MII. The underdeveloped Internet infrastructure in China has limited the growth of Internet usage in China. If the necessary Internet infrastructure is not developed, or is not developed on a timely basis, future growth of the Internet in China could be limited and our business could be harmed.

***We must rely on the Chinese government to develop China's Internet infrastructure and, if it does not develop this infrastructure, our ability to grow our business could be hindered.***

The Chinese government's interconnecting, national networks connect to the Internet through government-owned international gateways, which are the only channels through which a domestic Chinese user can connect to the international Internet network. We rely on this backbone and China Telecom and China Netcom to provide data communications capacity primarily through local telecommunications lines. Although the Chinese government has announced plans to aggressively develop the national information infrastructure, we cannot assure you that this infrastructure will be developed. In addition, we have no guarantee that we will have access to alternative networks and services in the event of any disruption or failure. If the necessary infrastructure standards or protocols or complementary products, services or facilities are not developed by the Chinese government, the growth of our business could be hindered.

***Our operations could be disrupted by unexpected network interruptions caused by system failures, natural disasters or unauthorized tampering with our systems.***

The continual accessibility of our websites and the performance and reliability of our network infrastructure are critical to our reputation and our ability to attract and retain users, advertisers and merchants. Any system failure or performance inadequacy that causes interruptions in the availability of our services or increases the response time of our services could reduce our appeal to advertisers and consumers. Factors that could significantly disrupt our operations include: system failures and outages caused by fire, floods, earthquakes, power loss, telecommunications failures and similar events; software errors; computer viruses, break-ins and similar disruptions from unauthorized tampering with our computer systems; and security breaches related to the storage and transmission of proprietary information, such as credit card numbers or other personal information.

We have limited backup systems and redundancy. Recently, we experienced an unauthorized tampering of the mail server of our China website which briefly disrupted our operations. Future disruptions or any of the foregoing factors could damage our reputation, require us to expend significant capital and other resources and expose us to a risk of loss or litigation and possible liability. We do not carry sufficient business interruption insurance to compensate for losses that may occur as a result of any of these events. Accordingly, our revenues and results of operations may be adversely affected if any of the above disruptions should occur.

***Future outbreaks of Severe Acute Respiratory Syndrome ( SARS ), Avian flu or other widespread public health problems could adversely affect our business.***

Future outbreaks of SARS, Avian flu or other widespread public health problems in China and surrounding areas, where most of our employees work, could negatively impact our business in ways that are hard to predict. Prior experience with the SARS virus suggests that a future outbreak of SARS, Avian flu or other widespread public health problems may lead public health authorities to enforce quarantines, which could result in closures of some of our offices and other disruptions of our operations. A future outbreak of SARS, Avian flu or other widespread public health problems could result in reduction of our advertising and fee-based revenues.

***Political and economic conditions in Greater China and the rest of Asia are unpredictable and may disrupt our operations if these conditions become unfavorable to our business.***

We expect to derive a substantial percentage of our revenues from the Greater China market. Changes in political or economic conditions in the region are difficult to predict and could adversely affect our operations or cause the Greater China market to become less attractive to advertisers, which could reduce our revenues. We maintain a strong local identity and presence in each of the regions in the Greater China market and we cannot be sure that we will be able to effectively maintain this local identity if political conditions were to change. Furthermore, many countries in Asia have experienced significant economic downturns since the middle of 1997, resulting in slower GDP growth for

the entire region as a result of higher interest rates and currency fluctuations. If declining economic growth rates persist in these countries, expenditures for Internet access, infrastructure improvements and advertising could decrease, which could negatively affect our business and our profitability over time.

Economic reforms in the region could also affect our business in ways that are difficult to predict. For example, since the late

**Table of Contents**

1970s, the Chinese government has been reforming the Chinese economic system to emphasize enterprise autonomy and the utilization of market mechanisms. Although we believe that these reform measures have had a positive effect on the economic development in China, we cannot be sure that they will be effective or that they will benefit our business.

***We issued \$100 million of zero coupon convertible subordinated notes due 2023, or possibly earlier upon a change of control, which we may not be able to repay in cash and could result in dilution of our basic earnings per share.***

In July 2003, we issued \$100 million of zero coupon convertible subordinated notes due July 15, 2023, first puttable to us on July 15, 2007. Each \$1,000 principal amount of the notes is convertible into 38.7741 shares of our ordinary shares prior to July 15, 2023 if the sale price of our ordinary shares issuable upon conversion of the notes reaches a specified threshold or specified corporate transactions have occurred. One of the conditions for conversion of the notes to SINA ordinary shares is that the market price of SINA ordinary shares reaches a specified threshold for a defined period of time. The specified thresholds are (i) during the period from issuance to July 15, 2022, if the sale price of SINA ordinary shares, for each of any five consecutive trading days in the immediately preceding fiscal quarter, exceeds 115% of the conversion price per ordinary share, and (ii) during the period from July 15, 2022 to July 15, 2023, if the sale price of SINA ordinary shares on the previous trading day is more than 115% of the conversion price per ordinary share. On July 15 annually from 2007 to 2013, and on July 15, 2018, or upon a change of control, holders of the notes may require us to repurchase all or a portion of the notes for cash. For the three months ended June 30, 2006, the sale price of SINA ordinary shares did not exceed the threshold set forth in Item (i) above for the required period of time. Therefore, the notes are not convertible into SINA ordinary shares during the three months ending September 30, 2006. Upon a conversion, we may choose to pay the purchase price of the notes in cash, ordinary shares, or a combination of cash and ordinary shares. We may not have enough cash on hand or have the ability to access cash to pay the notes if holders ask for repayment on the various put dates, or upon a change of control, or at maturity. In addition, the purchase of our notes with our ordinary shares or the conversion of the notes into our ordinary shares could result in dilution of our basic earnings per share.

***Currency fluctuations and restrictions on currency exchange may adversely affect our business, including limiting our ability to convert Chinese renminbi into foreign currencies and, if Chinese renminbi were to decline in value, reducing our revenues in U.S. dollar terms.***

Our reporting currency is the U.S. dollar and our operations in China, Hong Kong, Taiwan use their respective local currencies as their functional currencies. The majority of our revenues derived and expenses incurred are in Chinese renminbi with a relatively small amount in New Taiwan dollars, Hong Kong dollars and U.S. dollars. We are subject to the effects of exchange rate fluctuations with respect to any of these currencies. For example, the value of the renminbi depends to a large extent on Chinese government policies and China's domestic and international economic and political developments, as well as supply and demand in the local market. Since 1994, the official exchange rate for the conversion of renminbi to U.S. dollars had generally been stable and the renminbi had appreciated slightly against the U.S. dollar. However, on July 21, 2005, the Chinese government changed its policy of pegging the value of Chinese renminbi to the U.S. dollar. Under the new policy, Chinese renminbi may fluctuate within a narrow and managed band against a basket of certain foreign currencies. As a result of this policy change, Chinese renminbi appreciated approximately 2.5% against the U.S. dollar in 2005. It is possible that the Chinese government could adopt a more flexible currency policy, which could result in more significant fluctuation of Chinese renminbi against the U.S. dollar. We can offer no assurance that Chinese renminbi will be stable against the U.S. dollar or any other foreign currency.

The income statements of our international operations are translated into U.S. dollars at the average exchange rates in each applicable period. To the extent the U.S. dollar strengthens against foreign currencies, the translation of these foreign currencies denominated transactions results in reduced revenues, operating expenses and net income for our international operations. Similarly, to the extent the U.S. dollar weakens against foreign currencies, the translation of these foreign currency denominated transactions results in increased revenues, operating expenses and net income for our international operations. We are also exposed to foreign exchange rate fluctuations as we convert the financial statements of our foreign subsidiaries into U.S. dollars in consolidation. If there is a change in foreign currency

exchange rates, the conversion of the foreign subsidiaries' financial statements into U.S. dollars will lead to a translation gain or loss which is recorded as a component of other comprehensive income. In addition, we have certain assets and liabilities that are denominated in currencies other than the relevant entity's functional currency. Changes in the functional currency value of these assets and liabilities create fluctuations that will lead to a transaction gain or loss. We have not entered into agreements or purchased instruments to hedge our exchange rate risks, although we may do so in the future. The availability and effectiveness of any hedging transactions may be limited and we may not be able to successfully hedge our exchange rate risks.

Although Chinese governmental policies were introduced in 1996 to allow the convertibility of Chinese renminbi into foreign currency for current account items, conversion of Chinese renminbi into foreign exchange for capital items, such as foreign direct investment, loans or securities, requires the approval of the State Administration of Foreign Exchange, or SAFE, which is under the

**Table of Contents**

authority of the People's Bank of China. These approvals, however, do not guarantee the availability of foreign currency. We cannot be sure that we will be able to obtain all required conversion approvals for our operations or that Chinese regulatory authorities will not impose greater restrictions on the convertibility of Chinese renminbi in the future. Because a significant amount of our future revenues may be in the form of Chinese renminbi, our inability to obtain the requisite approvals or any future restrictions on currency exchanges could limit our ability to utilize revenue generated in Chinese renminbi to fund our business activities outside China, or to repay foreign currency obligations, including our debt obligations, which would have a material adverse effect on our financial conditions and results of operation.

***Changes to existing accounting pronouncements, including SFAS 123R, or taxation rules or practices may adversely affect our reported results of operations or how we conduct our business.***

A change in accounting pronouncements or taxation rules or practices can have a significant effect on our reported results and may even affect our reporting of transactions completed before the change is effective. Pursuant to SEC rules, we adopted the Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS 123R) starting January 1, 2006. SFAS 123R requires us to measure compensation costs for all share-based compensation (including stock options and our employee stock purchase plan, as currently constructed) at fair value and take compensation charges equal to that value. The method that we use to determine the fair value of stock options is based upon, among other things, the volatility of our ordinary shares. The price of our ordinary shares has historically been volatile. Therefore, the requirement to measure compensation costs for all share-based compensation under SFAS 123R could negatively affect our profitability and the trading price of our ordinary shares. SFAS 123R and the impact of expensing on our reported results could also limit our ability to continue to use stock options as an incentive and retention tool, which could, in turn, hurt our ability to recruit employees and retain existing employees. Other new accounting pronouncements or taxation rules and varying interpretations of accounting pronouncements or taxation practice have occurred and may occur in the future. This change to existing rules, future changes, if any, or the questioning of current practices may adversely affect our reported financial results or the way we conduct our business.

***We may be required to record a significant charge to earnings if we must reassess our goodwill or amortizable intangible assets arising from acquisitions.***

We are required under GAAP to review our amortizable intangible assets for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Goodwill is required to be tested for impairment at least annually. Factors that may be considered a change in circumstances indicating that the carrying value of our amortizable intangible assets may not be recoverable include a decline in stock price and market capitalization and slower growth rates in our industry. We may be required to record a significant charge to earnings in our financial statements during the period in which any impairment of our goodwill or amortizable intangible assets is determined. As of June 30, 2006, our goodwill and amortizable intangible assets arising from acquisitions were \$91.4 million.

In July 2006, China Mobile made changes to their policy on subscription-based MVAS (as described in the risk factor above titled *With respect to MVAS, we rely on China Mobile and China Unicom for service delivery, billing and fee collection.*). Such changes could significantly reduce the Company's ability to acquire new monthly MVAS subscribers and significantly increase the churn rate of existing monthly MVAS subscribers. The Company may need to assess goodwill and intangible related to the MVAS operation for impairment and may need to record a significant charge to earnings if an impairment is determined. As of June 30, 2006, goodwill and intangible related to the MVAS operation was \$69.4 million.

***While we believe that we currently have adequate internal control procedures in place, we are still exposed to potential risks from recent legislation requiring companies to evaluate controls under Section 404 of the Sarbanes-Oxley Act of 2002.***

While we believe that we currently have adequate internal control procedures in place, we are still exposed to potential risks from recent legislation requiring companies to evaluate controls under Section 404 of the Sarbanes-Oxley Act of 2002. Under the supervision and with the participation of our management, we have evaluated our internal controls systems in order to allow management to report on, and our registered independent public accounting firm to attest to, our internal controls, as required by Section 404 of the Sarbanes-Oxley Act. We have

performed the system and process evaluation and testing required in an effort to comply with the management certification and auditor attestation requirements of Section 404. As a result, we have incurred additional expenses and a diversion of management's time. If we are not able to continue to meet the requirements of Section 404 in a timely manner or with adequate compliance, we might be subject to sanctions or investigation by regulatory authorities, such as the SEC or the NASDAQ National Market. Any such action could adversely affect our financial results and the market price of our ordinary shares.

**Table of Contents**

***You should not place undue reliance on our financial guidance, nor should you rely on our quarterly operating results as an indication of our future performance because our results of operations are subject to significant fluctuations.***

We may experience significant fluctuations in our quarterly operating results due to a variety of factors, many of which are outside of our control. Significant fluctuations in our quarterly operating results could be caused by any of the factors identified in this section, including but not limited to our ability to retain existing users, attract new users at a steady rate and maintain user satisfaction; the announcement or introduction of new or enhanced services, content and products by us or our competitors; significant news events that increase traffic to our websites; technical difficulties, system downtime or Internet failures; demand for advertising space from advertisers; seasonality of the advertising market; the amount and timing of operating costs and capital expenditures relating to expansion of our business, operations and infrastructure; governmental regulation; seasonal trends in Internet use; a shortfall in our revenues relative to our forecasts and a decline in our operating results due to our inability to adjust our spending quickly; and general economic conditions and economic conditions specific to the Internet, electronic commerce and the Greater China market. As a result of these and other factors, you should not place undue reliance on our financial guidance, nor should you rely on quarter-to-quarter comparisons of our operating results as indicators of likely future performance. Our quarterly revenue and earnings per share guidance is our best estimate at the time we provide guidance. Our operating results may be below our expectations or the expectations of public market analysts and investors in one or more future quarters. If that occurs, the price of our ordinary shares could decline and you could lose part or all of your investment.

***Our stock price has been historically volatile and may continue to be volatile, which may make it more difficult for you to resell shares when you want at prices you find attractive.***

The trading price of our ordinary shares has been and may continue to be subject to considerable daily fluctuations. During the three months ended June 30, 2006, the closing sale prices of our ordinary shares on the NASDAQ National Market ranged from \$22.88 to \$29.24 per share and the closing sale price on August 4, 2006 was \$23.37 per share. Our stock price may fluctuate in response to a number of events and factors, such as quarterly variations in operating results, announcements of technological innovations or new products and media properties by us or our competitors, changes in financial estimates and recommendations by securities analysts, the operating and stock price performance of other companies that investors may deem comparable, new governmental restrictions or regulations and news reports relating to trends in our markets. In addition, the stock market in general, and the market prices for China-related and Internet-related companies in particular, have experienced extreme volatility that often has been unrelated to the operating performance of such companies. These broad market and industry fluctuations may adversely affect the price of our ordinary shares, regardless of our operating performance.

***We may be classified as a passive foreign investment company, which could result in adverse U.S. tax consequences to U.S. investors.***

Based upon the nature of our income and assets, we may be classified as a passive foreign investment company, or PFIC, by the United States Internal Revenue Service for U.S. federal income tax purposes. This characterization could result in adverse U.S. tax consequences to you. For example, if we are a PFIC, our U.S. investors will become subject to increased tax liabilities under U.S. tax laws and regulations and will become subject to more burdensome reporting requirements. The determination of whether or not we are a PFIC is made on an annual basis, and those determinations depend on the composition of our income and assets, including goodwill, from time to time. Although in the past we have operated our business and in the future we intend to operate our business so as to minimize the risk of PFIC treatment, you should be aware that certain factors that could affect our classification as PFIC are out of our control. For example, the calculation of assets for purposes of the PFIC rules depends in large part upon the amount of our goodwill, which in turn is based, in part, on the then market value of our shares, which is subject to change. Similarly, the composition of our income and assets is affected by the extent to which we spend the cash we have raised on acquisitions and capital expenditures. In addition, the relevant authorities in this area are not clear and so we operate with less than clear guidance in our effort to minimize the risk of PFIC treatment. Therefore, we cannot be sure whether we are not and will not be a PFIC for the current or any future taxable year. In the event we are determined to be a PFIC, our stock may become less attractive to U.S. investors, thus negatively impacting the price

of our stock.

***We have a single shareholder who can substantially influence the outcome of all matters voted upon by our shareholders and whose interests may not be aligned with yours.***

In February 2005, Shanda and several of its affiliates reported that they beneficially acquired 9,821,765 shares of our ordinary shares, which represents approximately 18.3% of our ordinary shares outstanding as of August 4, 2006. As a result, Shanda is able to substantially influence all matters requiring the approval of our shareholders, including the election of directors and the approval of



**Table of Contents**

significant corporate transactions such as acquisitions. This concentration of ownership could delay, defer or prevent a change in control or otherwise impede a merger or other business combination that the Board of Directors or other shareholders may view favorably. Additionally, in the event Shanda obtains Board representation, it may have influence over certain of the Company's business activities otherwise not subject to a shareholder vote.

*Anti-takeover provisions in our charter documents and SINA's shareholder rights plan may discourage our acquisition by a third party, which could limit our shareholders' opportunity to sell their shares at a premium.*

Our Amended and Restated Memorandum and Articles of Association include provisions that could limit the ability of others to acquire control of us, modify our structure or cause us to engage in change in control transactions. These provisions could have the effect of depriving shareholders of an opportunity to sell their shares at a premium over prevailing market prices by discouraging third parties from seeking to obtain control of us in a tender offer or from otherwise engaging in a merger or similar transaction with us.

For example, our Board of Directors has the authority, without further action by our shareholders, to issue up to 3,750,000 preference shares in one or more series and to fix the powers and rights of these shares, including dividend rights, conversion rights, voting rights, terms of redemption and liquidation preferences, any or all of which may be greater than the rights associated with our ordinary shares. Preference shares could thus be issued quickly with terms calculated to delay or prevent a change in control or make removal of management more difficult. In addition, if the Board of Directors issues preference shares, the market price of our ordinary shares may fall and the voting and other rights of the holders of our ordinary shares may be adversely affected. Similarly, the Board of Directors may approve the issuance of debentures convertible into voting shares, which may limit the ability of others to acquire control of us.

In addition, we have adopted a shareholder rights plan pursuant to which our existing shareholders would have the right to purchase ordinary shares from the Company at half the market price then prevailing in the event a person or group acquires more than 10% of our outstanding ordinary shares, or an additional 0.5% in the case of certain shareholders holding more than 10% at the time of the plan adoption, including Shanda and its affiliates, on terms our Board of Directors does not approve. As a result, such rights could cause substantial dilution to the holdings of the person or group which acquires more than 10%, or an additional 0.5%, as the case may be. Accordingly, the shareholder rights plan may inhibit a change in control or acquisition and could adversely affect a shareholder's ability to realize a premium over the then prevailing market price for the ordinary shares in connection with such a transaction.

**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**

On June 23, 2006, the Company held its Annual General Meeting of Shareholders. At the meeting, the shareholders elected as directors Yongji Duan (with 36,474,800 shares voting for and 10,766,850 shares withheld), Yan Wang (with 37,974,559 shares voting for and 9,267,091 shares withheld), Xiaotao Chen (with 37,996,892 shares voting for and 9,244,758 shares withheld), Charles Chao (with 37,998,693 shares voting for and 9,242,957 shares withheld) and Hurst Lin (with 37,968,228 shares voting for and 9,273,422 shares withheld).

The term of office of each of the following directors continued after the Annual General Meeting of Shareholders: Ter Fung Tsao, Song-Yi Zhang, Pehong Chen, Lip-Bu Tan and Yichen Zhang.

The shareholders ratified the appointment of PricewaterhouseCoopers Zhong Tian CPAs Limited Company as the independent auditors for the current fiscal year (with 37,998,343 shares voting for, 19,355 shares against and 9,223,951 shares abstaining).

**Item 5. Other Information**

None.

**Table of Contents**

**Item 6. Exhibits**

(a) Exhibits.

- 3.1 Amended and Restated Articles of Association of SINA Corporation (filed as Exhibit 3.1 to the Company's Annual Report on Form 10-K filed on March 16, 2005 and incorporated by reference herein).
- 3.2 Amended and Restated Memorandum of Association of SINA.com (filed as Exhibit 3.2 to the Company's Annual Report on Form 10-K filed on March 16, 2005 and incorporated by reference herein).
- 4.1 Form of Subordinated Note due July 15, 2023 (Filed as Exhibit 4.1 to the Company's Report on Form 10-Q for the three month period ended June 30, 2003, and incorporated herein by reference).
- 4.2 Indenture, dated as of July 7, 2003, by and between the Company and the Bank of New York (Filed as Exhibit 4.2 to the Company's Report on Form 10-Q for the three month period ended June 30, 2003, and incorporated herein by reference).
- 4.3 Registration Rights Agreement, dated as of July 7, 2003, by and between the Company and Credit Suisse First Boston LLC (Filed as Exhibit 4.3 to the Company's Report on Form 10-Q for the three month period ended June 30, 2003, and incorporated herein by reference).
- 4.4 Rights Agreement dated as of February 22, 2005 between SINA Corporation and American Stock Transfer & Trust Company, as Rights Agent (filed as Exhibit 4.1 to the Company's Report on Form 8-K filed on February 24, 2005, and incorporated herein by reference).
- 31.1\* Certificate of Chief Executive Officer pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2\* Certificate of Chief Financial Officer pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1\* Certificate of Chief Executive Officer pursuant to 18 U.S.C. section 1350.
- 32.2\* Certificate of Chief Financial Officer pursuant to 18 U.S.C. section 1350.

\* Filed herewith.

**Table of Contents**

**SIGNATURE**

Pursuant to the requirements 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.

SINA CORPORATION

Dated: August 9, 2006

By: /s/ Charles Chao  
Charles Chao  
President and Chief Executive Officer  
(Principal Executive Officer)

44

---

**Table of Contents**

SINA CORPORATION  
Exhibit Index

<b>Exhibit Number</b>	<b>Description</b>
3.1	Amended and Restated Articles of Association of SINA Corporation (filed as Exhibit 3.1 to the Company's Annual Report on Form 10-K filed on March 16, 2005 and incorporated by reference herein).
3.2	Amended and Restated Memorandum of Association of SINA.com (filed as Exhibit 3.2 to the Company's Annual Report on Form 10-K filed on March 16, 2005 and incorporated by reference herein).
4.1	Form of Subordinated Note due July 15, 2023 (Filed as Exhibit 4.1 to the Company's Report on Form 10-Q for the three month period ended June 30, 2003, and incorporated herein by reference).
4.2	Indenture, dated as of July 7, 2003, by and between the Company and the Bank of New York (Filed as Exhibit 4.2 to the Company's Report on Form 10-Q for the three month period ended June 30, 2003, and incorporated herein by reference).
4.3	Registration Rights Agreement, dated as of July 7, 2003, by and between the Company and Credit Suisse First Boston LLC (Filed as Exhibit 4.3 to the Company's Report on Form 10-Q for the three month period ended June 30, 2003, and incorporated herein by reference).
4.4	Rights Agreement dated as of February 22, 2005 between SINA Corporation and American Stock Transfer & Trust Company, as Rights Agent (filed as Exhibit 4.1 to the Company's Report on Form 8-K filed on February 24, 2005, and incorporated herein by reference).
31.1*	Certificate of Chief Executive Officer pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certificate of Chief Financial Officer pursuant to Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certificate of Chief Executive Officer pursuant to 18 U.S.C. section 1350.
32.2*	Certificate of Chief Financial Officer pursuant to 18 U.S.C. section 1350.

\* Filed herewith.