ASIAINFO HOLDINGS INC
Form 10-Q
August 07, 2009
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2009

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 001-15713

ASIAINFO HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**752506390**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

4TH FLOOR, ZHONGDIAN INFORMATION TOWER

6 ZHONGGUANCUN SOUTH STREET, HAIDIAN DISTRICT

BEIJING 100086, CHINA

(Address of principal executive offices, including zip code)

+8610 8216 6688

(Registrant s telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨ (Do not check if a smaller reporting company)	Smaller reporting company	¨

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

The number of shares outstanding of the registrant s common stock as of August 3, 2009 was 45,682,506.

Table of Contents

ASIAINFO HOLDINGS, INC.

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2009

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ASIAINFO HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

(In thousands, except share and per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008 As adjusted (1)	2009	2008 As adjusted (1)
Revenues:				
Software products and solutions	$ 47,151	$ 30,013	$ 89,588	$ 57,152
Service	5,931	4,209	10,930	7,550
Third-party hardware	5,486	7,836	9,026	12,362
Total revenues	58,568	42,058	109,544	77,064
Cost of revenues:				
Software products and solutions	22,609	13,660	40,823	24,816
Service	1,967	1,704	3,897	3,418
Third-party hardware	5,210	7,644	8,526	11,940
Total cost of revenues	29,786	23,008	53,246	40,174
Gross profit	28,782	19,050	56,298	36,890
Sales and marketing	9,929	8,212	20,466	16,107
General and administrative	3,652	2,248	7,218	4,857
Research and development	8,792	5,029	16,007	9,687
Total operating expenses	22,373	15,489	43,691	30,651
Income from operations	6,409	3,561	12,607	6,239
Other income				
Interest income	534	1,067	1,158	2,282
Dividend	3	84	174	303
Gain from sales of short-term investments	1,210	2,359	1,210	3,533
Other income (expenses), net	9	(256)	(14)	(530)
Total other income, net	1,756	3,254	2,528	5,588
Income before provisions for income taxes and discontinued operations	8,165	6,815	15,135	11,827
Income taxes expense	962	1,594	2,147	2,327
Income from continuing operations	7,203	5,221	12,988	9,500

Income from discontinued operations, net of taxes								980
Net income		7,203		5,221		12,988		10,480
Less: Net loss attributable to the noncontrolling interest		(2)				(7)		
Net income attributable to AsiaInfo Holdings, Inc.	$	7,205	$	5,221	$	12,995	$	10,480
Earnings per share:								
Income from continuing operations attributable to AsiaInfo Holdings, Inc. common stockholders:								
Basic	$	0.16	$	0.12	$	0.30	$	0.21
Diluted	$	0.16	$	0.11	$	0.29	$	0.20
Income from discontinued operations attributable to AsiaInfo Holdings, Inc. common stockholders:								
Basic	$		$		$		$	0.02
Diluted	$		$		$		$	0.02
Net income attributable to AsiaInfo Holdings, Inc. common stockholders:								
Basic	$	0.16	$	0.12	$	0.30	$	0.23
Diluted	$	0.16	$	0.11	$	0.29	$	0.22
Weighted average shares used in computation:								
Basic		44,586,996		45,094,860		44,048,268		44,944,271
Diluted		45,917,056		47,044,412		45,554,547		46,715,304
Amounts attributable to AsiaInfo Holdings, Inc. common stockholders:								
Income from continuing operations, net of tax		7,205		5,221		12,995		9,500
Income from discontinued operations, net of tax								980
Net income	$	7,205	$	5,221	$	12,995	$	10,480

(1) Amounts were extracted from Form 10-Q for the quarter ended June 30, 2008, as adjusted for adoption of Statement of Financial Accounting Standards No. 160 as set out in Note 1.

See accompanying notes to condensed consolidated financial statements.

Table of Contents

ASIAINFO HOLDINGS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)

(In thousands, except share and per share amounts)

	June 30, 2009	December 31, 2008 As adjusted (2)
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 177,470	$ 172,119
Restricted cash	11,853	12,510
Short-term investments held-to-maturity securities	10,555	
Short-term investments available-for-sale securities	24,821	28,633
Accounts receivable (net of allowances of $2,956 and $2,605 as of June 30, 2009 and December 31, 2008, respectively)	103,225	52,011
Inventories	7,477	12,322
Other receivables	3,190	2,813
Deferred income tax assets current	3,334	3,334
Prepaid expenses and other current assets	4,625	5,425
Total current assets	346,550	289,167
Long-term investment	4,696	4,696
Property and equipment, net	2,781	2,887
Other acquired intangible assets, net	2,629	3,008
Deferred income tax assets noncurrent	2,671	2,671
Goodwill	21,138	20,725
Total assets	$ 380,465	$ 323,154
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 54,334	$ 13,835
Accrued expenses	15,698	14,235
Deferred revenue	31,260	44,414
Accrued employee benefits	23,693	27,570
Other payables	7,410	5,288
Income taxes payable	298	646
Other taxes payable	5,908	6,311
Deferred income tax liabilities	1,085	934
Total current liabilities	139,686	113,233
Unrecognized tax benefits	2,127	1,326
Other long-term liabilities	135	135
Total liabilities	141,948	114,694
Commitments and contingencies (Note 21)		
Stockholders Equity:		

Common stock (100,000,000 shares authorized; $0.01 par value; 48,683,113 shares and 46,466,170 shares issued as of June 30, 2009 and December 31, 2008, respectively; 45,683,113 shares and 43,466,170 shares outstanding as of June 30, 2009 and December 31, 2008, respectively)	487	464
Additional paid-in capital	231,932	215,948
Treasury stock, at cost (3,000,000 shares and 3,000,000 shares as of June 30, 2009 and December 31, 2008, respectively)	(27,749)	(27,749)
Statutory reserve	17,212	17,212
Accumulated deficit	(2,571)	(15,566)
Accumulated other comprehensive income	19,155	18,093
Total AsiaInfo Holdings, Inc. stockholders equity	238,466	208,402
Noncontrolling interest	51	58
Total stockholders equity	238,517	208,460
Total liabilities and stockholders equity	$ 380,465	$ 323,154

(2) December 31, 2008 balances were extracted from audited financial statements, as adjusted for adoption of Statement of Financial Accounting Standards No. 160 as set out in Note 1.

See accompanying notes to condensed consolidated financial statements.

2

Table of Contents

ASIAINFO HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(In thousands, except share and per share amounts)

	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
Cash flows from operating activities:		
Net income	$ 12,988	$ 10,480
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization of property and equipment	657	589
Stock-based compensation expenses	5,040	1,340
Amortization of other acquired intangible assets	629	845
(Gain) loss on disposal of property and equipment	(5)	32
Gain from sales of available-for-sale securities	(1,210)	(3,533)
Provision for bad debt	492	188
Gain on sales of discontinued operations		(1,515)
Proceeds from sales of trading securities		121
Purchase of trading securities		(76)
Acquisition related costs	(12)	
Changes in operating assets and liabilities:		
Accounts receivable	(51,706)	(1,174)
Inventories	4,845	(3,777)
Other receivables	(378)	(174)
Deferred income taxes		(624)
Prepaid expenses and other current assets	800	(144)
Accounts payable	40,499	1,251
Accrued expenses	1,489	214
Deferred revenue	(13,154)	6,709
Accrued employee benefits	(3,876)	(4,440)
Other payables	2,310	(119)
Other taxes payable	(403)	450
Income taxes payable	452	(2,210)
Net cash (used in) provided by operating activities	(543)	4,433
Cash flows from investing activities:		
Decrease (increase) in restricted cash	656	(1,176)
Purchases of available-for-sale securities		(3,068)
Purchases of held-to-maturity securities	(10,555)	
Proceeds from sales of available-for-sale securities	6,211	7,320
Proceeds from sales of held-to-maturity securities		1,541
Purchases of property and equipment	(510)	(531)
Proceeds from disposal of property and equipment	5	7
Purchase of businesses, net of cash acquired	(872)	(1,502)
Proceeds from disposal of discontinued operations		1,515
Long-term equity investment	(25)	
Net cash (used in) provided by investing activities	(5,090)	4,106
Cash flows from financing activities:		
Proceeds from exercise of stock options	10,967	3,115
Repurchase of common stock		(1,664)

Net cash provided by financing activities	10,967	1,451
Effect of exchange rate changes on cash and cash equivalents	17	4,452
Net increase in cash and cash equivalents	5,351	14,442
Cash and cash equivalents at beginning of period	172,119	148,834
Cash and cash equivalents at end of period	$ 177,470	$ 163,276

See accompanying notes to condensed consolidated financial statements.

Table of Contents

ASIAINFO HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

(In thousands, except share and per share amounts)

	AsiaInfo Holdings, Inc. Stockholders									
	Common Stock						Accumulated Other			
	Outstanding Shares	Amount	Additional Paid-in Capital	Treasury Stock	Statutory Reserve	Accumulated Deficit	Comprehensive Income	Noncontrolling Interest	Total Equity	Comprehensive Income
Balance at January 1, 2009	43,466,170	$ 464	$ 215,948	$ (27,749)	$ 17,212	$ (15,566)	$ 18,093	$ 58	$ 208,460	
Net income						5,790		(5)	5,785	$ 5,785
Other comprehensive income:										
Foreign currency translation adjustments							(97)		(97)	(97)
Net unrealized gain/(loss) on available-for-sale investments, net of tax effects of $ (578)							1,180		1,180	1,180
Comprehensive income										$ 6,868
Stock option exercises	205,514	2	1,622						1,624	
Performance-based restricted stock units vesting	239,880	3	(3)							
Share-based compensation (restricted stock units)			181						181	
Share-based compensation (performance-based restricted stock units)			1,001						1,001	
Balance at March 31, 2009	43,911,564	$ 469	$ 218,749	$ (27,749)	$ 17,212	$ (9,776)	$ 19,176	$ 53	$ 218,134	
Net income						7,205		(2)	7,203	$ 7,203
Other comprehensive income:										
Foreign currency translation adjustments							69		69	69
Transfer to income statement of realized (gain)/loss on available-for-sale investments, net of tax effects of $350							(860)		(860)	(860)
Net unrealized gain/(loss) on available-for-sale investments, net of tax effects of $77							770		770	770
Comprehensive income										$ 7,182
Stock option exercises	1,299,160	13	9,330						9,343	
Performance-based restricted stock units vesting	472,089	5	(5)							
Restricted stock unit vesting	300									
Share-based compensation (restricted stock units)			190						190	
Share-based compensation (performance-based restricted stock units)			3,668						3,668	

Balance at June 30, 2009	45,683,113	$ 487	$ 231,932	$ (27,749)	$ 17,212	$ (2,571)	$ 19,155	$ 51	$ 238,517

See accompanying notes to condensed consolidated financial statements.

Table of Contents

ASIAINFO HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

(In thousands, except share and per share amounts)

1. BASIS OF PREPARATION

(a) The accompanying unaudited condensed consolidated financial statements include the accounts of AsiaInfo Holdings, Inc., its subsidiaries, and its variable interest entities (the VIEs) (collectively, the Company). All significant intercompany balances and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X, as promulgated by the Securities and Exchange Commission (the SEC). Accordingly, they do not include all of the information and notes required by US GAAP for completing annual financial statements. However, management believes that the disclosures are adequate to ensure the information presented is not misleading. US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, contingencies and results of operations. While management has based their assumptions and estimates on the facts and circumstances existing as of June 30, 2009, final amounts may differ from these estimates.

In the opinion of the management of the Company, the accompanying unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, which are necessary for a fair presentation of the results for the interim periods presented. These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s audited financial statements on Form 10-K for the fiscal year ended December 31, 2008. The results of operations for the interim periods presented are not indicative of the operating results to be expected for any subsequent interim period or for the Company s fiscal year ending December 31, 2009.

AsiaInfo Holdings, Inc. uses the United States (U.S.) dollar as its reporting currency and functional currency. The financial records of the Company s People s Republic of China (PRC) subsidiaries and VIEs are maintained in Renminbi (RMB), their functional currency and the currency of the PRC. Their balance sheets are translated into U.S. dollars based on the exchange rate quoted by the People s Bank of China as of the balance sheet date. Their statements of operations are translated using a weighted average exchange rate for the period. Translation adjustments are reflected in accumulated other comprehensive income in stockholders equity.

The RMB is not freely convertible into U.S. dollars or other currencies. All foreign exchange transactions involving RMB must take place through the People s Bank of China or other institutions authorized to buy and sell foreign currencies. The exchange rates adopted for the foreign exchange transactions are the rates of exchange quoted by the People s Bank of China.

(b) The accompanying unaudited condensed consolidated financial statements have been prepared using the same accounting policies as used in the preparation of the Company s consolidated financial statements on Form 10-K for the fiscal year ended December 31, 2008 except for the following additional accounting policies:

(1) Newly adopted Accounting Pronouncements

Effective January 1, 2009, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 160, Noncontrolling Interests in Consolidated Financial Statements An Amendment of ARB No. 51 (SFAS 160), which was retrospectively applied, requires noncontrolling interests to be separately presented as a component of stockholders equity on the unaudited condensed consolidated financial statements.

Effective April 1, 2009, the Company adopted Financial Accounting Standards Board (FASB) Staff Position No. FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments (FAS 107-1 and APB 28-1). FAS 107-1 and APB 28-1 amend FASB Statement No. 107, Disclosures about Fair Value of Financial Instruments, to require disclosures about fair value of financial instruments for interim reporting periods as well as in annual financial statements of publicly traded companies. FAS 107-1 and APB 28-1 also amend APB Opinion No. 28, Interim Financial Reporting, to require those disclosures in summarized financial information at interim reporting periods. The Company believes the adoption of this standard did not have any significant impact on its financial condition or results of operations.

Effective April 1, 2009, the Company adopted FASB Staff Position No. FAS 115-2 and FAS 124-2, Recognition and Presentation of Other-Than-Temporary Impairments (FAS 115-2 and FAS 124-2). FAS 115-2 and FAS 124-2 amend the other-than-temporary impairment guidance in U.S. GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. The Company believes the adoption of this standard did not have any significant impact on its financial condition or results of operations.

Effective April 1, 2009, the Company adopted FASB Staff Position No. FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly (FAS 157-4). FAS 157-4 provides additional guidance for estimating fair value in accordance with FASB Statement No. 157, Fair Value Measurements, when the volume and level of activity for the asset or liability have significantly decreased. FAS 157-4 also includes guidance on identifying circumstances that indicate a transaction is not orderly. FAS 157-4 emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under the then current market conditions. The Company believes the adoption of this standard did not have any significant impact on its financial condition or results of operations.

Effective April 1, 2009, the Company adopted SFAS No. 165, Subsequent Events (SFAS 165). The objective of SFAS 165 is to establish general standards for the accounting and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. In particular, SFAS 165 sets forth the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements; the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements; and the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. The Company believes the adoption of this standard did not have any significant impact on its financial condition or results of operations.

(2) Revenue recognition

The Company s Lenovo-AsiaInfo information security products are accounted for under the American Institute of Certified Public Accountants (AICPA) Statement of Position No. 97-2, Software Revenue Recognition (SOP 97-2) because the related software is considered to be more than incidental and is essential to the functionality of the related equipment. The Lenovo-AsiaInfo information security products are sold with bundled post-contract customer support (PCS) services over a term of one, two or three years.

For contracts entered into before December 31, 2008, the Company recognized total arrangement fee for the information security products as revenue upon delivery assuming all other revenue recognition criteria were met regardless of whether the PCS services terms are one, two or three years because (a) PCS services primarily included telephone and online support, (b) PCS services were substantially provided within the first year of the arrangement term, (c) the costs of providing PCS services had historically been insignificant and are expected to be insignificant in the future, and (d) PCS services did not include upgrades or enhancements. PCS services provided beyond the first year of the service term had historically been negligible. The Company accrued the estimated costs of providing PCS services upon delivery of the Lenovo-AsiaInfo information security software products.

For contracts entered into after January 1, 2009, the Company extended PCS services terms so that the PCS services terms include unspecified upgrades. In addition, the Company has established the vendor-specific objective evidence of fair value of the PCS services. Therefore, the security products revenue is recognized upon the delivery and the PCS services revenue is deferred and recognized ratably over the PCS services period.

Recently Issued Accounting Pronouncements Not Yet Adopted

On June 12, 2009, the FASB issued Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) (SFAS 167). SFAS 167 is a revision to FIN 46(R) and changes how a company determines whether an entity should be consolidated when such entity is insufficiently capitalized or is not controlled by the company through voting (or similar rights). The determination of whether a company is required to consolidate an entity is based on, among other things, the entity s purpose and design and the company s ability to direct the activities of the entity that most significantly impact the entity s economic performance. SFAS 167 retains the scope of FIN 46(R) but added entities previously considered qualifying special purpose entities, or QSPEs, since the concept of these entities is eliminated in SFAS 166. SFAS 167 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2009. The Company does not expect the adoption of SFAS 167 to have a significant effect on its consolidated financial position or results of operations.

At its July 1, 2009 meeting, the FASB ratified the consensus reached on EITF Issue No.09-1 Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing (EITF 09-1). EITF No. 09-1 applies to share lending arrangements with an entity s own shares when executed in contemplation of a convertible debt offering or other financing. The share lending arrangement is required to be measured at fair value and recognized as an issuance cost associated with the convertible debt offering or other financing. If counterparty default is probable, then the share lender is required to recognize an expense equal to the then fair value of the unreturned shares, net of the fair value of probable recoveries. Entities will be required to apply EITF 09-1 in periods beginning on or after June 15, 2009, for share lending arrangements entered into in those periods. The Company does not expect the adoption of EITF 09-1 to have a significant effect on its consolidated financial position or results of operations

2. FINANCIAL INSTRUMENTS

Financial instruments consist of cash and cash equivalents, restricted cash, short-term investments, accounts receivable, other receivables, other payables, income taxes payable, other taxes payable and long-term investments in equity securities of unquoted companies.

Short-term investments are classified as available-for-sale securities, held-to-maturity securities and trading securities, as discussed in Note 4.

Certain long-term investments have been written down to their fair values, as of December 31, 2008, as discussed in Note 7. The fair values of other long-term investments, which are carried at cost, are not readily determinable.

Table of Contents

The carrying values of other financial instruments approximate their fair values due to the short-term nature of these instruments. The Company does not use derivative instruments to manage risks.

3. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash on hand, demand deposits and highly liquid investments, which are unrestricted as to withdrawal or use, and which have remaining maturities of three months or less when purchased.

4. SHORT-TERM INVESTMENTS

Short-term investments are classified as available-for-sale securities, held-to-maturity securities and trading securities

As of June 30, 2009, the Company s held-to-maturity securities consist of term deposits carried at cost of $10,555. The term deposits are either not allowed to be redeemed early or are subject to penalty for early redemption before their maturity. The carrying amounts of the held-to-maturity securities approximate their fair values due to their short-term nature. No held-to-maturity securities were held as of December 31, 2008.

As of June 30, 2009 and December 31, 2008, the Company did not hold trading securities.

The following table provides additional information concerning the Company s available-for-sale securities, which consist principally of corporate stocks, bond funds, and stock funds issued by major financial institutions.

	June 30, 2009				December 31, 2008			
	Cost (1)	Gross unrealized gains	Gross unrealized losses	Fair value	Cost (1)	Gross unrealized gains	Gross unrealized losses	Fair value
Bond funds	$ 16,801	$ 669	$	$ 17,470	$ 16,785	$ 984	$	$ 17,769
Stock funds	5,812	1,453		7,265	10,808	8		10,816
Corporate stocks	48	38		86	48			48
Total	$ 22,661	$ 2,160	$	$ 24,821	$ 27,641	$ 992	$	$ 28,633

(1) Cost is net of nil and $4,684 impairment loss as of June 30, 2009 and December 31, 2008, respectively, which represent the decline in fair value of the available-for-sale securities. The Company determined that such decline was other-than-temporary, based on various factors such as continuing challenging global financial markets, poor performance of the global equity markets, and the duration and the extent to which the fair value of the investment had continued to be less than the cost.

Where applicable, the Company uses quoted prices in active markets for identical assets or liabilities (Level 1 investments) to determine the fair value of trading and available-for-sale securities. If quoted prices in active markets for identical assets or liabilities are not available to determine fair value, then the Company uses quoted prices for similar assets and liabilities or inputs other than the quoted prices that are observable either directly or indirectly, which are included in Level 2 investments. The Company did not have Level 2 investments as of June 30, 2009. The Company s Level 3 investments other than derivatives primarily include investments in certain mutual funds without quoted prices as of the date of reporting. The Company values its Level 3 investments using the quoted market price as of the most recent priced day prior to the date of reporting because the Company believes the fair value of the investments would not have materially changed during the 10-day period between the pricing date and the date of reporting.

The available-for-sale securities measured and recorded at fair value on a recurring basis as of June 30, 2009 were as follows:

	Fair Value Measurements at the Reporting Date Using
	Total Balance

	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Bond funds	$ 17,470	$	$	$ 17,470
Stock funds			7,265	7,265
Corporate stocks	86			86
Total	$ 17,556	$	$ 7,265	$ 24,821

Table of Contents

The following table presents changes in Level 3 stock funds measured on a recurring basis for the six-month period ended June 30, 2009:

	As at June 30, 2009
Beginning balance	$ 5,812
Unrealized gain	1,453
Ending balance	$ 7,265

The following table provides additional information on the realized gains of the Company during the three-month and six-month periods ended June 30, 2009. For purpose of determining gross realized gains, the cost of securities sold is based on specific identification.

	Three Months Ended June 30,					
	2009			2008		
	Proceeds	Costs	Gains	Proceeds	Costs	Gains
Available-for-sale securities	$ 6,211	$ 5,001	$ 1,210	$ 4,993	$ 2,605	$ 2,388
Trading securities				45	24	21
Total	$ 6,211	$ 5,001	$ 1,210	$ 5,038	$ 2,629	$ 2,409

	Six Months Ended June30,					
	2009			2008		
	Proceeds	Costs	Gains	Proceeds	Costs	Gains
Available-for-sale securities	$ 6,211	$ 5,001	$ 1,210	$ 7,320	$ 3,782	$ 3,538
Trading securities				121	76	45
Total	$ 6,211	$ 5,001	$ 1,210	$ 7,441	$ 3,858	$ 3,583

The Company reported nil and $50 impairment losses for its short-term investments for the six-month periods ended June 30, 2009 and 2008, respectively. The Company reported no impairment losses for its short-term investments for the three-month periods ended June 30, 2009 and 2008.

5. ACCOUNTS RECEIVABLE

Accounts receivable balances included both billed and unbilled amounts. Revenue recognized in excess of billings is recorded as unbilled receivables. All billed and unbilled amounts are expected to be collected within one year. Accounts receivable balances included bank acceptance drafts receivable and commercial acceptance drafts receivable. These bank acceptance drafts and commercial acceptance drafts were non-interest bearing and were due within six months of issuance.

The components of accounts receivable as of June 30, 2009 and December 31, 2008 were as follows:

	June 30, 2009	December 31, 2008
Billed accounts receivable	$ 50,990	$ 23,438
Unbilled accounts receivable	54,488	29,057
Bank acceptance drafts	95	38
Commercial acceptance drafts	608	2,083
Less: accounts receivable allowance	(2,956)	(2,605)
Total accounts receivable, net	$ 103,225	$ 52,011

6. INVENTORIES

The components of inventories as of June 30, 2009 and December 31, 2008 were as follows:

	June 30, 2009	December 31, 2008
Raw materials	$ 896	$ 824
Finished goods	6,581	11,498
Total	$ 7,477	$ 12,322

7. LONG-TERM INVESTMENTS

(a) In October 2005, the Company acquired five percent of the outstanding equity interests of Hinge Software Company Limited (Hinge), a Shanghai-based provider of business intelligence software solutions. The Company uses the cost method of accounting in accordance with APB 18 to record its investment in Hinge since the Company does not have the ability to exercise significant influence over the operating and financial policies of Hinge. Due to the global financial crisis in 2008, Hinge s business dropped significantly causing a significant decline in Hinge s fair value. The Company determined that its investment in Hinge became worthless as of December 31, 2008 and that the decline in the fair value was other-than-temporary. Consequently, during the year ended December 31, 2008, the Company recognized an impairment loss of $2,042, which was equal to the carrying amount of the investment.

Table of Contents

(b) On September 12, 2008, the Company acquired 2,170,000 redeemable convertible Series B Preferred Shares of C-Platform Corporation (C-Platform), for a total cash consideration of $4,696, including $52 in transaction costs. The total consideration had been paid as of September 30, 2008. Following the transaction, the Company owned approximately 19.9% of C-Platform s issued and outstanding share capital, or 17% of C-Platform s share capital on a fully-diluted basis. Since the Company does not have the ability to exercise significant influence over the operating and financial policies of C-Platform, the Company uses the cost method of accounting in accordance with APB 18 to record its investment in C-Platform.

C-Platform is a Cayman Islands company, which, through its subsidiaries in China, provides data operating services, a form of value-added telecommunications services, to telecommunications operators in China. The Company believes that the transaction furthers its on-going strategy of expanding its market leading telecommunications software solutions business in China.

8. ACQUISITION

In April 2009, the Company, through its majority-owned subsidiary Shanghai Xinjia Information and Technology Co., Ltd., acquired certain operating assets and liabilities of Shanghai Huanyou Information Consultation Co. Ltd., a PRC based provider of value-added telecommunications services, for a cash consideration of $658. Goodwill acquired through this acquisition was $410. The acquisition was accounted for as a business acquisition because the Company believes the acquired assets constituted a business according to SFAS No. 141(R). The Company believes that the transaction furthers its ongoing strategy of expanding its market-leading telecommunications software solutions business in China.

9. GOODWILL

The changes in the carrying amount of goodwill by reporting segments during the six months ended June 30, 2009 were as follows:

	June 30, 2009		
	AsiaInfo Technologies	Lenovo-AsiaInfo	Total
Beginning balance	$ 18,186	$ 2,539	$ 20,725
Goodwill obtained in acquisitions of businesses	410		410
Foreign exchange difference due to translation	3		3
Ending balance	$ 18,599	$ 2,539	$ 21,138

10. OTHER ACQUIRED INTANGIBLE ASSETS, NET

	June 30, 2009				December 31, 2008			
	Gross carrying amount	Accumulated amortization	Foreign exchange difference	Net carrying amount	Gross carrying amount	Accumulated amortization	Foreign exchange difference	Net carrying amount
Core technologies	$ 2,331	$ (2,227)	$	$ 104	$ 2,331	$ (2,133)	$	$ 198
Trade names	341	(294)		47	341	(279)		62
Contract backlogs	2,451	(2,463)	12		2,451	(2,463)	12	
Customer lists	131	(104)	12	39	131	(89)	12	54
Customer relationships	2,740	(1,584)	280	1,436	2,593	(1,277)	279	1,595
Distribution network	870	(870)			870	(859)		11
Software	1,758	(1,308)	153	603	1,758	(1,159)	153	752
Non-compete agreements	446	(155)	22	313	436	(122)	22	336
Corporate business agency agreement	91	(4)		87				
	$ 11,159	$ (9,009)	$ 479	$ 2,629	$ 10,911	$ (8,381)	$ 478	$ 3,008

The future amortization expenses for the net carrying amount of intangible assets with definite lives as of June 30, 2009 are expected to be as follows:

2009	$ 632
2010	1,077
2011	535
2012	200
2013	185
	$ 2,629

9

Table of Contents

11. COMPREHENSIVE INCOME

The components of comprehensive income during the three and six months ended June 30, 2009 and 2008 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Net income	$ 7,203	$ 5,221	$ 12,988	$ 10,480
Transfer to income statement of realized (gain)/loss on available-for-sale investments - net of tax effects of $350 and $599, $350 and $887 for the three and six months ended June 30, 2009 and 2008, respectively	(860)	(1,789)	(860)	(2,651)
Net unrealized gain/(loss) on available-for-sale investments, net of tax effects of $77 and $1,300, $(501) and $1,691 for the three and six months ended June 30, 2009 and 2008, respectively	770	(1,912)	1,950	(7,532)
Change in cumulative foreign currency translation adjustment	69	2,652	(28)	7,315
Comprehensive income	7,182	4,172	14,050	7,612
Comprehensive income/(loss) attributable to noncontrolling interest	(2)		(7)	
Comprehensive income attributable to AsiaInfo Holdings, Inc.	$ 7,184	$ 4,172	$ 14,057	$ 7,612

12. CREDIT FACILITIES

As of June 30, 2009, the Company had short-term credit facilities for working capital purposes totaling $34,637 expiring in March 2010. As of June 30, 2009, the credit facilities were secured by bank deposits of $11,000 and credit facilities of $3,545 were pledged as security for issuing standby letters of credit and accounts payable to hardware suppliers and customers. As of June 30, 2009, unused short-term credit facilities were $31,092. In addition, the Company had standby letters of credit and bank acceptance drafts as of June 30, 2009, which were collateralized by bank deposits of $853. Total bank deposits pledged as security for credit facilities, standby letters of credit, and bank acceptance drafts totaled $11,853 as of June 30, 2009 and were presented as restricted cash in the consolidated balance sheets. As of December 31, 2008, the Company had total short-term credit facilities totaling $34,631, which will expire in December 2009 and were secured by bank deposits of $11,336.

13. DISCONTINUED OPERATIONS

In January 2007, the Company sold certain assets and liabilities constituting its financial services IT solutions business (FIS), which is grouped under the Company s Lenovo-AsiaInfo reportable segment, to Fidelity Information Systems (Fidelity) , a major U.S.-based provider of IT services and information products to financial institutions, for a maximum cash consideration valued at $3,581 (RMB25,430), which was structured as follows: (1) $1,653 (RMB11,740) was received from Fidelity upon closing; (2) $413 (RMB2,934) escrow amount was transferred to an escrow agent by Fidelity upon closing; and (3) $1,515 (RMB 10,756) was to be paid subject to adjustment based upon an earn-out calculation and certain contingencies.

On March 18, 2008, the Company received the $1,515 contingent payment from Fidelity and recognized the amount as gain on sale of discontinued operations. Certain cost which was related to the contingent payment and amounting to $209 (RMB1,483) was accrued accordingly.

The accompanying condensed consolidated statements of operations reflect FIS as discontinued operations. Results of the FIS discontinued operations are summarized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Gain on sales of discontinued operations	$	$	$	$ 1,306
Provision for income taxes				(326)

Gain on discontinued operations	$	$	$	$	980

14. ACCOUNTS PAYABLE

Accounts payable included bank acceptance drafts payable of $1,772 and $2,328 and commercial acceptances payable of $11 and $216 as of June 30, 2009 and December 31, 2008, respectively. These bank acceptance drafts and commercial acceptances were non-interest bearing and were due within six months of issuance.

Table of Contents

15. VALUE-ADDED TAXES REBATE

Revenue from software products and solutions includes the benefit of the rebate of value-added taxes on sales of software and services received from the Chinese tax authorities as part of the PRC government s policy of encouraging software development in the PRC. The rebate totaled $2,151 and $2,908 for the three months ended June 30, 2009 and 2008, respectively.

16. INCOME TAXES

The Company is subject to U.S. federal and state income taxes and the Company s subsidiaries and VIEs incorporated in the PRC are subject to PRC income taxes.

Reconciliation between the provision for income taxes computed by applying the U.S. federal tax rate to income before income taxes and the actual provision for income taxes is as follows:

	Six Months Ended June 30, 2009	2008
U.S. federal rate	35%	35%
Difference between statutory rate and foreign effective tax rate	(28)	(27)
Change in valuation allowance		1
Subpart F income inclusion	1	2
Stock-based compensation	5	2
Qualified Electing Fund income	1	7
	14%	20%

During the six months ended June 30, 2009, the Company recorded a discrete tax benefit of $634 as a result of true ups of certain research and development tax deductions (super R&D deductions) claimed by certain of its PRC subsidiaries for the tax year 2008.

During the six months ended June 30, 2009, the Company recorded an additional long term tax liability of approximately $760 for certain tax positions it has taken on certain 2008 tax filings relating to the uncertainties as to the deductibility of certain expenses.

Aggregate undistributed earnings of approximately $55,542 at June 30, 2009 of the Company s subsidiaries and VIEs located in the PRC that are available for distribution to the Company are considered to be indefinitely reinvested under APB opinion No. 23, and accordingly, no provision has been made for the Chinese dividend withholding taxes that would be payable upon the distribution of those amounts to the Company. Additionally, the Chinese tax authorities have clarified that distributions made out of pre-January 1, 2008 retained earnings would not be subject to the withholding tax. The Company has not qualified the deferred income tax liability that would arise if earnings in the second quarter were to be distributed or were determined to be no longer permanently reinvested.

The Company is subject to taxation in the U.S. and various states and foreign jurisdictions. There is one ongoing examination by the Hong Kong taxing authority at this time. The Company believes that it has not taken any aggressive filing positions in its Hong Kong tax filings and it is expecting that it will not be subject to additional tax liabilities or penalties. There are no ongoing examinations by other taxing authorities at this time. The Company s various tax years from 2000 to 2009 remain open in these taxing jurisdictions.

17. STOCK-BASED COMPENSATION

2002 Stock Option Plan and the Prior Plans

Under the Company s 2002 Stock Option Plan (the 2002 Plan), the Company was authorized to grant options for the purchase of up to 4,500,000 shares of common stock to employees, directors and consultants at prices not less than the fair market value on the date of grant for incentive stock options and nonqualified options. Shares as to which an option is granted under the 2002 Plan but remains unexercised at the expiration, forfeiture or other termination of such option may be the subject of the grant of further options. Prior to adopting the 2002 Stock Option Plan, the Company adopted annual stock option plans for each of 1995, 1996, 1997, 1998, 1999 and 2000 (such plans, together with the 2002 Stock Option Plan, are referred to hereinafter as the Option Plans).

The vesting periods of the options under the Option Plans are determined based on individual stock option agreements. Options granted prior to 1998 generally vest and become exercisable over three years at an equal annual rate. Exercise terms of options granted in 1998, 1999, 2000 and 2002 are substantially similar to those of options granted prior to 1998 except that the vesting and exercise periods are generally over four one-year cliffs at an annual rate of 20%, 20%, 30% and 30% for the 1999 plan, generally over four years at an annual rate of 25% for the 2000 plan, and are generally no more than four years at an annual rate of 25% for the 2002 Plan.

Activities for the Option Plans are summarized as follows:

	Number of shares	Weighted average exercise price per share	Aggregate Intrinsic Value
Outstanding, January 1, 2009	3,356,752	$ 9.14	
Granted			
Forfeited	(550)	8.45	
Exercised	(205,514)	7.90	
Outstanding, March 31, 2009	3,150,688	9.22	
Granted			
Forfeited	(25,100)	4.21	
Exercised	(1,299,160)	7.19	
Outstanding, June 30, 2009	1,826,428	10.74	$ 14,849
Vested and expected to vest, June 30, 2009	1,826,428	10.74	14,849
Exercisable, June 30, 2009	1,826,428	$ 10.74	$ 14,849

Table of Contents

The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the closing stock price of $17.21 of the Company s common stock on the last trading day on June 30, 2009.

Total intrinsic value of options exercised for each of the three months ended June 30, 2009 and 2008 was $15,255 and $2,274, respectively.

As of June 30, 2009, there was no unrecognized share-based compensation cost relating to share options.

2005 Stock Incentive Plan- restricted stock units (RSUs)

Under the Company s 2005 Stock Incentive Plan (the 2005 Plan), the Company may grant participants restricted stock awards, stock options, or other types of equity incentives. The number of shares authorized for issuance is (a) 600,000 shares plus (b) any authorized shares of Common Stock that, as of April 21, 2005, were available for issuance under the Company s 2002 Plan, or that thereafter become available for issuance under the 2002 Plan in accordance with its terms.

A restricted stock unit (RSU) is an agreement to issue stock at the time when the award vests. These units are vested on an annual basis equally over four years, 25% on each anniversary of the grant date. The fair value of each RSU is measured on the grant date based on the market price of the stock on the grant date. The Company also has the right, in its sole discretion, to pay cash in lieu of the issuance of vested shares of common stock. No such cash payment right was exercised by the Company.

RSUs as of June 30, 2009 and changes during the three months ended June 30, 2009 were as follows:

	Number of shares	Weighted average grant date fair value
Restricted stock units unvested at January 1, 2009	147,812	$ 5.42
Granted	70,500	9.59
Vested		
Forfeited	(525)	4.05
Restricted stock units unvested at March 31, 2009	217,787	6.78
Granted	10,000	18.80
Vested	(300)	4.86
Forfeited		
Restricted stock units unvested at June 30, 2009	227,487	$ 7.31

Total intrinsic value of RSUs exercised for each of the three months ended June 30, 2009 and 2008 was $5.5 and $37, respectively.

As of June 30, 2009, there was $1,251 unrecognized share-based compensation cost related to RSUs. That unrecognized cost is expected to be recognized over a weighted-average vesting period of 1.2 years. To the extent the actual forfeiture rate is different from the original estimate; the actual share-based compensation related to these awards may be different from the expectation.

2005 Stock Incentive Plan- performance-based restricted stock units (PSUs)

In November 2006, the Compensation Committee of the Board of Directors of the Company approved a stock unit award program under the 2005 Plan, permitting the Company to grant no more than 2,213,068 shares of performance-based restricted stock units (PSUs). 1,995,000 PSUs were granted in November 2006. Unlike the Company s RSUs, PSUs vest based on certain performance-based criteria, including annual earnings before interest and tax, annual net revenue growth and average stock closing price, provided the award holder continues to be an employee of the Company at the time the performance goals are met. Each PSU represents the contingent right of the participant to receive a payment in respect of a share of the Company s common stock. The Company also has the right, in its sole discretion, to pay cash in lieu of the issuance of vested shares of common stock. No such cash payment right was exercised by the Company.

Performance based PSUs as of June 30, 2009 and changes during the three months ended June 30, 2009 were as follows:

	Number of shares	Weighted average grant date fair value
Performance-based restricted stock units unvested at January 1, 2009	626,911	$ 5.05
Granted		
Vested		
Forfeited	(3,250)	4.99
Performance-based restricted stock units unvested at March 31, 2009	623,661	5.05
Granted		
Vested	(472,089)	5.05
Forfeited	(151,572)	5.05
Performance-based restricted stock units unvested at June 30, 2009		$

12

Table of Contents

Market based PSUs as of June 30, 2009 and changes during the three months ended June 30, 2009 were as follows:

	Number of shares	Weighted average grant date fair value
Market-based restricted stock units unvested at January 1, 2009	241,130	$ 2.14
Granted		
Vested	(239,880)	2.14
Forfeited	(1,250)	2.14
Market-based restricted stock units unvested at March 31, 2009		$

2008 Stock Incentive Plan

On February 25, 2008, the Board of Directors of the Company authorized the 2008 Stock Incentive Plan, as amended (the 2008 Plan). The 2008 Plan was subsequently approved by the Company s stockholders at the 2008 annual meeting of stockholders. Under the 2008 Plan, the Company may grant participants restricted stock awards, stock options, or other types of equity incentives. The number of shares authorized for issuance is (a) 2,000,000 shares plus (b) any authorized shares of the Company s common stock that, as of February 25, 2008, were available for issuance under the Company s 2005 Plan, or that thereafter become available for issuance under the 2005 Plan in accordance with its terms.

As of June 30, 2009, 1,669,400 PSUs were granted under the 2008 Plan. These awards will vest based on certain performance-based criteria, such as the Company s operating margin annual growth rate, provided the award holder continues to be an employee of the Company at the time the performance goals are met. Each PSU represents the contingent right of the participant to receive a payment in respect of a share of the Company s common stock, whether in shares, cash, or a combination thereof, subject to the terms and conditions of individual performance stock unit agreement. The Company also has the right, in its sole discretion, to pay cash in lieu of the issuance of vested shares of common stock. No such cash payment right was exercised by the Company.

	Number of shares	Weighted average grant date fair value
Performance-based restricted stock units unvested at January 1, 2009		$
Granted	1,649,400	13.10
Vested		
Forfeited		
Performance-based restricted stock units unvested at March 31, 2009	1,649,400	13.10
Granted	20,000	18.80
Vested		
Forfeited	(3,000)	13.10
Performance-based restricted stock units unvested at June 30, 2009	1,666,400	$ 13.17

Total intrinsic value of the PSUs granted under the 2005 Plan and the 2008 Plan and vested for the three months ended June 30, 2009 and 2008 was $8,125 and $5,218, respectively.

As of June 30, 2009, there was $3,414 unrecognized share-based compensation cost related to the PSUs granted under the 2008 Plan. This deferred cost is expected to be recognized over a weighted-average vesting period of 0.25 years. To the extent the actual forfeiture rate is different from the original estimate, the actual share-based compensation related to these awards may be different from the expectation.

The amount of stock-based compensation attributable to cost of revenues, sales and marketing, general and administrative expenses, and research and development is included in those line items on the face of the statement of operations. For the three-month and six-month periods ended June 30, 2009 and 2008, stock-based compensation expenses related to the stock options, the RSUs and the PSUs under SFAS 123(R) were allocated as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Cost of revenues	$ 1,102	$ 123	$ 1,395	$ 277
Sales and marketing	1,099	240	1,450	482
General and administrative	1,067	180	1,427	352
Research and development	590	107	768	229
Total stock-based compensation expense	$ 3,858	$ 650	$ 5,040	$ 1,340

Table of Contents

18. EARNINGS PER SHARE

The following is a reconciliation of the numerators and denominators of the basic and diluted net income per share computations:

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Six months Ended June 30, 2009	Six months Ended June 30, 2008
Amounts attributable to AsiaInfo Holdings, Inc. common stockholders (numerator)				
Income from continuing operations, net of taxes	$ 7,205	$ 5,221	$ 12,995	$ 9,500
Income from discontinued operations, net of taxes				980
Net income	$ 7,205	$ 5,221	$ 12,995	$ 10,480
Shares (denominator)				
Weighted average common stock outstanding				
Basic	44,586,996	45,094,860	44,048,268	44,944,271
Dilutive effect of stock-based compensation	1,330,060	1,949,552	1,506,279	1,771,033
Diluted	45,917,056	47,044,412	45,554,547	46,715,304
Earnings per share				
Net income from continuing operations attributable to AsiaInfo Holdings, Inc. common stockholders				
Basic	$ 0.16	$ 0.12	$ 0.30	$ 0.21
Diluted	$ 0.16	$ 0.11	$ 0.29	$ 0.20
Net income from discontinued operations attributable to AsiaInfo Holdings, Inc. common stockholders				
Basic	$	$	$	$ 0.02
Diluted	$	$	$	$ 0.02
Net income attributable to AsiaInfo Holdings, Inc. common stockholders				
Basic	$ 0.16	$ 0.12	$ 0.30	$ 0.23
Diluted	$ 0.16	$ 0.11	$ 0.29	$ 0.22

As of June 30, 2009 and 2008, the Company had 415,600 and 670,215 common stock options outstanding, respectively, that were excluded from the computation of diluted earnings per share (EPS), as their exercise prices exceeded the average market values in those periods. These options could potentially have a dilutive effect on EPS in the future.

19. SEGMENT INFORMATION

Since October 2004, the Company has been organized as two business units, AsiaInfo Technologies, encompassing the Company s traditional telecommunications business, and Lenovo-AsiaInfo, providing IT services, including security products and services, IT consulting, software customization, and business process outsourcing services, to the enterprise market in China. After disposing of certain non-core business lines during 2005 and 2006, Lenovo-AsiaInfo now focuses on IT security solutions for the small and medium-sized enterprise market in China. In accordance with the guidance of SFAS 131, the Company determined that each of these two business units represents an operating segment, of which discrete financial information is available and is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. Each operating segment has three product lines: (1) software products and solutions, (2) services, and (3) third-party hardware.

The Company s chief operating decision making group is the Company s Business Committee, comprising the Company s Chief Executive Officer, Chief Financial Officer and its senior management team, who allocate resources and evaluate performance of segments based on the following table of condensed statement of operations and total assets. Accordingly, other items such as inter-segment sales, interest income (expense), income tax expenses (benefit), depreciation and amortization are not disclosed by segment, since such information is not used by the Company s chief operating decision making group to assess the operating performance of individual segments.

The following is a condensed statement of operations and total assets for the Company s operating segments based on the Company s three major product lines:

	Three Months Ended June 30,					
	2009			2008		
	AsiaInfo Technologies	Lenovo-AsiaInfo	Total	AsiaInfo Technologies	Lenovo-AsiaInfo	Total
Revenue:						
Software products and solutions	$ 41,776	$ 5,375	$ 47,151	$ 25,875	$ 4,138	$ 30,013
Services	5,883	48	5,931	4,042	167	4,209
Third-party hardware	5,039	447	5,486	6,834	1,002	7,836
Total revenue:	52,698	5,870	58,568	36,751	5,307	42,058
Cost of revenues:						
Software products and solutions	20,275	2,334	22,609	12,230	1,430	13,660
Services	1,892	75	1,967	1,636	68	1,704
Third-party hardware	4,786	424	5,210	6,492	1,152	7,644
Total cost of revenues	26,953	2,833	29,786	20,358	2,650	23,008
Gross Profit	25,745	3,037	28,782	16,393	2,657	19,050
Segment expenses:						
Sales and marketing	7,569	2,360	9,929	5,956	2,256	8,212
General and administrative(1)	727	(78)	649	101	34	135
Research and development	7,787	1,005	8,792	4,465	564	5,029
Total segment expenses	16,083	3,287	19,370	10,522	2,854	13,376
Contribution profit (loss)	$ 9,662	$ (250)	$ 9,412	$ 5,871	$ (197)	$ 5,674

14

Table of Contents

	Six Months Ended June 30, 2009 AsiaInfo Technologies	2009 Lenovo-AsiaInfo	2009 Total	2008 AsiaInfo Technologies	2008 Lenovo-AsiaInfo	2008 Total
Revenue:						
Software products and solutions	$ 81,158	$ 8,430	$ 89,588	$ 50,327	$ 6,825	$ 57,152
Services	10,730	200	10,930	7,346	204	7,550
Third-party hardware	7,963	1,063	9,026	11,157	1,205	12,362
Total revenue:	99,851	9,693	109,544	68,830	8,234	77,064
Cost of revenues:						
Software products and solutions	37,189	3,634	40,823	22,511	2,305	24,816
Services	3,740	157	3,897	3,310	108	3,418
Third-party hardware	7,564	962	8,526	10,599	1,341	11,940
Total cost of revenues	48,493	4,753	53,246	36,420	3,754	40,174
Gross Profit	51,358	4,940	56,298	32,410	4,480	36,890
Segment expenses:						
Sales and marketing	15,985	4,481	20,466	11,841	4,266	16,107
General and administrative(1)	1,453	44	1,497	678	47	725
Research and development	14,082	1,925	16,007	8,575	1,112	9,687
Total segment expenses	31,520	6,450	37,970	21,094	5,425	26,519
Contribution profit (loss)	$ 19,838	$ (1,510)	$ 18,328	$ 11,316	$ (945)	$ 10,371

	As of June 30, 2009 AsiaInfo Technologies	As of June 30, 2009 Lenovo-AsiaInfo	As of June 30, 2009 Total	As of December 31, 2008 AsiaInfo Technologies	As of December 31, 2008 Lenovo-AsiaInfo	As of December 31, 2008 Total
Total assets (2)	$ 332,735	$ 47,730	$ 380,465	$ 270,595	$ 52,559	$ 323,154

(1) General and administrative expenses reported reflect only the direct controllable expenses of each business unit and do not include allocation of corporate general and administrative expenses. The credit amount in AsiaInfo-Technologies segment primarily reflect the results of certain bad debt provision reversals recorded in the three months ended June 30, 2008.

(2) Included in total assets are net accounts receivable of $98,412 and $4,813 for AsiaInfo Technologies and Lenovo-AsiaInfo, 2009, respectively, at June 30, 2009 and $46,194 and $5,817 for AsiaInfo Technologies and Lenovo-AsiaInfo, respectively, at December 31, 2008.

The following is a reconciliation of operating segment contribution profit to income before provision for income taxes:

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
Total contribution profit for reportable segments	$ 9,412	$ 5,674	$ 18,328	$ 10,371
Corporate general and administrative expenses	(3,003)	(2,113)	(5,721)	(4,132)
Interest income	534	1,067	1,158	2,282
Gain from sales of short term investments	1,210	2,409	1,210	3,583
Impairment losses on short term investments		(50)		(50)

Dividend	3	84	174	303
Other income (expense), net	9	(256)	(14)	(530)
Income before provision for income taxes and discontinued operations	$ 8,165	$ 6,815	$ 15,135	$ 11,827

15

Table of Contents

Since revenues net of cost of third-party hardware sales were reported to the chief operating decision maker, the Company also provides the following table, which reconciles revenues net of cost of third-party hardware sales to total revenues as presented in the consolidated statements of operations:

	Three Months Ended June 30,					
	2009			2008		
	AsiaInfo Technologies	Lenovo-AsiaInfo	Total	AsiaInfo Technologies	Lenovo-AsiaInfo	Total
Revenues net of cost of third-party hardware sales	$ 47,912	$ 5,446	$ 53,358	$ 30,259	$ 4,155	$ 34,414
Third-party hardware cost	4,786	424	5,210	6,492	1,152	7,644
Total revenues	$ 52,698	$ 5,870	$ 58,568	$ 36,751	$ 5,307	$ 42,058

	Six Months Ended June 30,					
	2009			2008		
	AsiaInfo Technologies	Lenovo-AsiaInfo	Total	AsiaInfo Technologies	Lenovo-AsiaInfo	Total
Revenues net of cost of third-party hardware sales	$ 92,287	$ 8,731	$ 101,018	$ 58,231	$ 6,893	$ 65,124
Third-party hardware cost	7,564	962	8,526	10,599	1,341	11,940
Total revenues	$ 99,851	$ 9,693	$ 109,544	$ 68,830	$ 8,234	$ 77,064

20. RELATED PARTIES TRANSACTIONS

The Company entered into a series of contractual agreements with Lenovo in connection with the acquisition of Lenovo s non-telecommunications IT services business in October 2004. In conjunction with that acquisition, the Company delivered 5,472,414 shares of its common stock to Lenovo. Among them, 648,769 shares were returned to the Company from an escrow account in February 2007. As of June 30, 2009, Lenovo owned approximately 9 percent of the Company s outstanding common stock.

The following table provides a summary of the Company s transactions with Lenovo during the three-month and six-month periods ended June 30, 2009 and 2008, respectively:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Sales and marketing	$ 14	$ 16	$ 28	$ 35
Research and development		1		2
Total operating expenses	$ 14	$ 17	$ 28	$ 37

	As of June 30, 2009	As of December 31, 2008
Balances with related parties:		
Other receivables	$ 225	$ 226
Deferred revenue	365	365
Other payables	782	782

21. COMMITMENTS AND CONTINGENCIES

Product warranty The Company s product warranty accrual reflected management s best estimate of probable liability under its product warranties. Management determines the warranty accrual based on historical experience and other currently available evidence. Product warranty accrual was recorded as a component of accrued expenses in the accompanying balance sheets.

Changes in the product warranty accrual for the six months period ended June 30, 2009 were as follows

		As of June 30, 2009
Balance at beginning of the period	$	418
Current period provision		12
Payments		(1)
Expired warranty		(146)
Foreign exchange difference		
Balance at end of the period	$	283

16

Litigation On December 4, 2001, a securities class action case was filed in New York City against the Company, certain of its officers and directors and the underwriters of the Company s initial public offering (IPO). The lawsuit alleged violations of the U.S. federal securities laws and was docketed in the United States District Court for the Southern District of New York as Hassan v. AsiaInfo Holdings, Inc., et al. The lawsuit alleged, among other things, that the underwriters of the Company s IPO improperly required their customers to pay the underwriters excessive commissions and to agree to buy additional shares of the Company s common stock in the aftermarket as conditions of their purchasing shares in the Company s IPO. The lawsuit further claimed that the alleged practices of the underwriters should have been disclosed in the Company s IPO prospectus and registration statement. The suit seeks rescission of the plaintiffs alleged purchases of the Company s common stock as well as unspecified damages. In addition to the case against the Company, various other plaintiffs had filed approximately 1,000 other, substantially similar class action cases (collectively, the IPO Allocation Cases) against approximately 300 other publicly traded companies and their IPO underwriters in New York City, which along with the case against the Company, had all been transferred to a single federal district judge for purposes of case management.

In April of 2009, the Company and most of the other issuer defendants in the IPO Allocation Cases reached a definitive agreement with the plaintiffs and the underwriter defendants to settle the IPO Allocation Cases. The definitive agreement was filed with the court on April 2, 2009 and was preliminarily approved by the court on June 10, 2009. It remains subject to final approval by the court. If the settlement is approved, the Company expects any damages payable to the plaintiffs to be fully funded by its directors and officers liability insurance policies. If the litigation proceeds, the Company intends to continue to defend the litigation vigorously. Moreover, if the litigation proceeds, the Company believes that the underwriters may have an obligation to indemnify the Company for the legal fees and other costs of defending this suit and that its directors and officers liability insurance policies would also cover the defense and potential exposure in the suit.

In addition, the Company received a letter dated July 30, 2007 from a putative stockholder demanding that the Company investigate and prosecute a claim for alleged short-swing trading in violation of Section 16(b) of the Exchange Act by the underwriters of the Company s IPO and certain of the Company s unidentified directors, officers and stockholders. On October 9, 2007, the putative stockholder commenced a civil lawsuit in the U.S. District Court for the Western District of Washington against Morgan Stanley and Deutsche Bank, two of the lead underwriters of the Company s IPO, alleging violations of Section 16(b) of the Exchange Act. The complaint alleges that the combined number of shares of the Company s common stock beneficially owned by the lead underwriters and certain unnamed officers, directors and principal stockholders exceeded ten percent of the Company s outstanding common stock from the date of the Company s IPO on March 3, 2000, through at least March 2, 2001. It further alleges that those entities and individuals were thus subject to the reporting requirements of Section 16(a) and the short-swing trading prohibition of Section 16(b), and failed to comply with those provisions. The complaint seeks to recover from the lead underwriters any short-swing profits obtained by them in violation of Section 16(b). None of the Company s directors, officers or stockholders is named as defendants in this action, although the Company is named as a nominal defendant. On July 25, 2008, the Company filed a joint motion to dismiss, with several other issuers who are also named as nominal defendants in the action. On March 12, 2009, the court granted the issuer defendants joint motion to dismiss without prejudice on the grounds that the plaintiff failed to make an adequate demand to the Company prior to filing her complaint. The plaintiff filed a Notice of Appeal on April 10, 2009.

The Company intends to continue to defend vigorously the two litigation matters described above. While the Company cannot guarantee the outcome of these proceedings, the Company believes that the final results of these lawsuits will have no material effect on the Company s consolidated financial condition, results of operations or cash flows.

22. STOCK REPURCHASE PROGRAM

From the commencement of the Company s first stock repurchase program, which was approved by the Company s Board of Directors in the fourth quarter of 2004, through December 31, 2005, the Company repurchased a total of 5,274,231 shares of its common stock at a total cost of $27,282.

On January 11, 2006, the Company announced the authorization of a stock repurchase program pursuant to which the Company was entitled, from time to time during a ninety-day period (expired on April 11, 2006), to purchase up to 4,000,000 shares of its common stock. As of April 11, 2006, the Company repurchased 2,095,208 shares of its common stock at a total cost of $9,563.

On April 25, 2006, the Company s Board of Directors authorized an extension to the 2006 repurchase program for an additional 90 days, from April 25, 2006 to July 24, 2006, but did not change the aggregate number of shares subject to repurchase under the 2006 repurchase program. As of July 18, 2006, the Company repurchased 1,904,792 shares of its common stock at a total cost of $8,223 pursuant to the extension of this repurchase program. The 2006 stock repurchase program, as extended, was completed on July 18, 2006.

All common stock repurchased by the Company under the 2005 and 2006 repurchase programs were reported as treasury stock. Of the total shares repurchased, 4,498,130 shares were issued to Lenovo in 2005 as part of the consideration for acquiring Lenovo-AsiaInfo. On June 27, 2006 and September 29, 2006, the Company s Board of Directors authorized the retirement of 3,799,109 and 976,992 shares of treasury stock, respectively. The retired shares resumed the status of authorized and unissued shares of the Company. As of December 31, 2006, the Company had no remaining treasury stock.

On September 11, 2007, the Company announced the authorization of a stock repurchase program under which the Company was entitled to repurchase up to 3,000,000 shares of its outstanding common stock. Pursuant to that program, the Company was entitled, from time to time for a period of four months, depending on market conditions, share price and other factors, to make one or more purchases, on the open market, or in privately negotiated transactions, subject to availability, of up to 3,000,000 shares of its outstanding common stock. As of December 31, 2007, the Company repurchased 244,300 shares of its common stock at a total cost of $1,953 pursuant to this repurchase program.

On February 27, 2008, the Company s Board of Directors authorized an extension to the 2007 repurchase program through July 10, 2008. Under the extended program, the Company was authorized to repurchase up to 2,755,700 shares of its outstanding common stock, from time to time, depending on market conditions, share price and other factors, on the open market or in privately negotiated transactions. Any common stock repurchased by the Company became part of its treasury stock and may be retired or used by the Company to finance or execute acquisitions or other arrangements. As of July 10, 2008, the Company had repurchased 166,400 shares of its common stock at a total cost of $1,664 pursuant to this extended repurchase program.

On September 17, 2008, the Company announced a stock repurchase program under which the Company was authorized to repurchase up to 3,000,000 shares of its outstanding common stock. As of December 31, 2008, the Company had repurchased 2,589,300 shares of its common stock at a total cost of $24,132 pursuant to this repurchase program. No stock was repurchased during the three-month period ended June 30, 2009. All common stock repurchased by the Company under the 2007 and 2008 repurchase programs were reported as treasury stock. As of June 30, 2009, the Company had 3,000,000 shares of treasury stock.

Table of Contents

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

Except for historical information, the statements contained in this quarterly report on Form 10-Q are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. The Private Securities Litigation Reform Act of 1995, or the Reform Act, contains certain safe harbors regarding forward-looking statements. Certain of the forward-looking statements include management s expectations, intentions and beliefs with respect to our growth, our operating results, the nature of the industry in which we are engaged, our business strategies and plans for future operations, our needs for capital expenditures, capital resources and liquidity, and similar expressions concerning matters that are not historical facts. Such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in the statements. All forward-looking statements included in this report are based on information available to us on the date hereof, and we assume no obligation to update any such forward-looking statements. These cautionary statements are being made pursuant to the provisions of the Reform Act with the intention of obtaining the benefits of the safe harbor provisions of the Reform Act. The factors that could cause actual results to differ materially include, but are not limited to, the factors discussed below under Item 1A. Risk Factors in Part II Other Information.

In this report, AsiaInfo, the Company, we, us and our refer to AsiaInfo Holdings Inc., its subsidiaries and consolidated variable interest entit

Overview

We are a leading provider of high-quality telecommunications software solutions and IT security products and services in China. In the telecommunications market, our software and services enable our customers to build, maintain, operate, manage and continuously improve their communications infrastructure. Our largest customers are the major telecommunications carriers in China and their provincial subsidiaries. In addition to providing customized software solutions to China s telecommunications carriers, we also offer sophisticated IT security products and services to many small and medium sized companies and government agencies in China.

We commenced our operations in the US in 1993 and moved our major operations from the US to China in 1995. We began generating significant network solutions revenues in 1996 and significant software revenues in 1998. We conduct the bulk of our business through our operating subsidiaries, most of which are Chinese companies.

We have derived, and believe that we will continue to derive, a significant portion of our revenues from a limited number of large telecommunications customers, such as China Mobile, China Unicom and China Telecom. The following table shows our revenues and percentage of total revenues derived from those three customers for the three-month periods ended June 30, 2009 and 2008.

	Three Month Ended June 30,			
	2009		2008	
	Revenues (in thousands)	Percentage of Total Revenues	Revenues (in thousands)	Percentage of Total Revenues
China Mobile	$ 38,206	65%	$ 26,907	64%
China Unicom*	9,510	16	8,212	20
China Telecom	4,966	9	1,740	4
Total	$ 52,682	90%	$ 36,859	88%

* Also includes revenues generated from China Netcom, which was merged with China Unicom on October 15, 2008.

As a result of our reliance on our key customers in the telecommunications industry, our operating results are influenced by governmental spending policies in that sector. Historically, a number of state-mandated restructurings in China s telecommunications sector have led to cancellation or delays in telecommunications-related capital expenditure, and have negatively impacted our operating results in certain periods. However, certain state-mandated restructurings in China s telecommunications sector have caused our revenues to increase as carriers have increased spending on software and IT infrastructure designed to increase their competitiveness. Any future restructurings affecting our major telecommunications customers may result in delays or cancellation of telecommunications-related spending, which could have an adverse impact on our business.

Since our acquisition of the non-telecommunications-related IT services business of Lenovo in October 2004, we have been organized as two business divisions: AsiaInfo Technologies, encompassing our traditional telecommunications business, and Lenovo-AsiaInfo, providing IT security products and services to China s enterprise market. For financial reporting purposes, each of the two business divisions is further organized into three product lines:

software products and solutions;

Table of Contents

services; and

third-party hardware.

Revenues

We report our revenues on the basis of the three principal types of revenues derived from our business: software products and solutions revenue, service revenue and third-party hardware revenue. Please refer to Note 19 to the condensed consolidated financial statements included in this report for detailed financial information regarding segment reporting.

Software products and solutions revenue. We typically sell our software as part of a total solutions package for our customers, which includes proprietary software licenses, professional services related to the design and implementation of the solutions (such as consulting, training, technical support and maintenance) and, in cases where the customer requests a turn-key solution, related hardware. Software products and solutions revenue includes two types of revenues: software license revenue and software services revenue. Software license revenue consists of fees received from customers for licenses or sublicenses to use our software products or third-party software products in perpetuity, typically up to a specified maximum number of users. In most cases where a customer is required to purchase additional licenses from us because the number of users exceeds the number of licensed users, we enter into an extension agreement with the customer to expand and upgrade the customer s system. These extension contracts will usually include a license for the additional users, updated versions of our software and, if required, additional services and hardware for the customer s network. Our software license revenue also includes the benefit of value-added tax rebates on software license sales, which reflect the Chinese government s policy of encouraging the development of China s software industry. Software services revenue consists of revenue from software installation, customization, training and other services. We also record reductions from revenue for our estimates of expected software sales returns from distributors based on current sales and historical sales returns.

Service revenue. Service revenue consists of revenue from professional services, including IT services, management consulting, and revenues for network planning, design, systems integration and training services.

In addition, in recent periods we have begun to generate service revenues by acting as a sales agent for International Business Machines Corporation, or IBM, or its distributors, for certain products sold to China Mobile (the IBM Arrangement). The service fee under this arrangement is determined as a percentage of the gross contract amount. We have evaluated the criteria outlined in Emerging Issue Task Force, or EITF, No. 99-19, Reporting Revenue Gross as Principal Versus Net as an Agent, when determining whether we would record as revenues the gross amount billed to China Mobile and related costs or the net amount earned after deducting hardware costs paid to the vendor, even though we bear inventory risks after the vendor ships the products to us and we bill gross amounts to China Mobile. We record the net amount earned after deducting hardware costs as agency service revenue because (1) the vendor is the primary obligor in these transactions, (2) we have no latitude in establishing the prices, (3) we are not involved in the determination of the product specifications, (4) we do not bear credit risk because we are contractually obligated to pay the vendor only when China Mobile pays us, and (5) we do not have the right to select suppliers.

Third-party hardware revenue. Other than the IBM Arrangement, we sometimes procure for, and sell hardware to, our customers as part of certain turn-key solutions. We typically minimize our exposure to hardware inventory risks by sourcing equipment from hardware vendors against letters of credit from our customers. For these hardware transactions, we have also evaluated the criteria outlined in EITF No. 99-19. As a result of the evaluation, we record the gross amounts billed to our customers as revenues because (1) we are the primary obligor in these transactions, (2) we bear the inventory risk, (3) we have latitude in establishing prices, (4) we are involved in the determination of the product specifications, (5) we bear credit risk, and (6) we have the right to select suppliers. As the telecommunications-related IT services market in China develops, our customers are increasingly purchasing hardware directly from hardware vendors and retaining us for our software and professional services.

Net revenue (Non-GAAP). Although we report our revenue on a gross basis, inclusive of hardware acquisition costs, we manage our business internally based on revenues net of hardware costs, or net revenues (Non-GAAP), which is consistent with our strategy of providing our customers with high-value IT professional services and, where efficient, outsourcing lower-end services such as hardware acquisition and installation. This strategy may result in lower growth rates for total revenue as against prior periods, but will not adversely impact revenue net of hardware costs. The following table shows our revenue breakdown on this basis and reconciles our net revenues (Non-GAAP) to total revenues:

	Reconciliation of Net Revenues (Non-GAAP) to Total Revenues	
	Three Months Ended June 30,	
	2009	**2008**

	AsiaInfo Technologies	Lenovo-AsiaInfo	Total	AsiaInfo Technologies	Lenovo-AsiaInfo	Total
			(In thousands)			
Revenues net of hardware costs:						
Software products and solutions revenue	$ 41,776	$ 5,375	$ 47,151	$ 25,875	$ 4,138	$ 30,013
Service revenue	5,883	48	5,931	4,042	167	4,209
Third-party hardware revenue net of hardware costs	253	23	276	342	(150)	192
Total revenues net of hardware costs	47,912	5446	53,358	30,259	4,155	34,414
Total hardware costs	4,786	424	5,210	6,492	1,152	7,644
Total revenues	$ 52,698	$ 5,870	$ 58,568	$ 36,751	$ 5,307	$ 42,058

Table of Contents

	Reconciliation of Net Revenues (Non-GAAP) to Total Revenues Six Months Ended June 30,					
	2009			2008		
	AsiaInfo Technologies	Lenovo-AsiaInfo	Total	AsiaInfo Technologies	Lenovo-AsiaInfo	Total
	(In thousands)					
Revenues net of hardware costs:						
Software products and solutions revenue	$ 81,158	$ 8,430	$ 89,588	$ 50,327	$ 6,825	$ 57,152
Service revenue	10,730	200	10,930	7,346	204	7,550
Third-party hardware revenue net of hardware costs	399	101	500	558	(136)	422
Total revenues net of hardware costs	92,287	8,731	101,018	58,231	6,893	65,124
Total hardware costs	7,564	962	8,526	10,599	1,341	11,940
Total revenues	$ 99,851	$ 9,693	$ 109,544	$ 68,830	$ 8,234	$ 77,064

We believe total revenues net of hardware costs in each of the segments of our business more accurately reflect our core business, which is the provision of software solutions and services, and provides transparency to our investors. We believe this measure provides transparency to our investors because it is the measure used by our management to evaluate the competitiveness and performance of our business in each of the segments. In addition, third-party hardware revenue tends to fluctuate from period to period depending on the requirements of our customers. As a result, a presentation that excludes hardware costs allows investors to better evaluate the performance of our core business and we report this presentation to our chief operating decision maker.

Cost of Revenues

Software products and solutions costs. Software products and solutions costs consist primarily of three components:

- packaging and written manual expenses for our proprietary software products and solutions;
- compensation and travel expenses for the professionals involved in modifying, customizing or installing our software products and solutions and in providing consultation, training and support services; and
- software license fees paid to third-party software providers for the right to sublicense their products to our customers as part of our solutions offerings.

The costs associated with designing and further developing our proprietary software are classified as research and development expenses as incurred.

Service costs. Service costs consist primarily of compensation and travel expenses for the professionals involved in designing and implementing IT services, management consulting and network solutions projects.

Third-party hardware costs. We recognize hardware costs in full upon delivery of the hardware to our customers. In order to minimize our working capital requirements, we generally obtain from our hardware vendors payment terms that are timed to permit us to receive payment from our customers for the hardware before our payments to hardware vendors are due. However, in large projects we sometimes obtain less favourable payment terms from our customers, thereby increasing our working capital requirements.

Amortization of intangible assets, depreciation of properties and equipments, and rental expenses are also included in cost of revenue.

Operating Expenses

Operating expenses are comprised of sales and marketing expenses, research and development expenses, general and administrative expenses and impairment of goodwill and intangible assets. Compensation expenses consistently comprise a significant portion of our total operating expenses.

Sales and marketing expenses include compensation expenses for employees in our sales and marketing departments, third-party advertising expenses, sales commissions and sales consulting fees, as well as the depreciation and amortization expenses allocated to our sales and marketing departments.

Research and development expenses relate to the development of new software and the modification of existing software. We expense such costs as they are incurred.

Taxes

Except for certain hardware procurement and resale transactions, we conduct substantially all of our business through our Chinese subsidiaries and variable interest entities, or VIEs. Prior to the enactment of China s new Chinese Enterprise Income Tax Law, or the EIT Law, which became effective on January 1, 2008, foreign-invested enterprises, or FIEs, were generally subject to a 30% state enterprise income tax plus a 3% local income tax. However, most of our operating subsidiaries in China, as FIEs, were entitled to tax holidays or certain preferential tax treatments, which thus reduced their effective rate of income tax to 15% or lower in some cases. Since the EIT Law became effective, all resident enterprises are subject to a flat 25% income tax rate, unless they are otherwise eligible for certain preferential tax treatments under the new rules.

Pursuant to the implementation rules to the EIT Law issued in December 2007, and several subsequent transition rules, certain of our subsidiaries in China can continue to enjoy preferential tax rates as long as they are qualified as High and New Technology Enterprises, or HNTEs. Some of our subsidiaries and VIEs in China became subject to a normal 25% income tax rate, while certain of our subsidiaries and VIEs in China remain eligible for the lower rates under the transition rules. The HNTE status allows qualifying entities to be eligible for a 15% tax rate for three years. At the conclusion of the three-year period, the qualifying enterprise has the option to renew its HNTE status for an additional three years through a simplified application process if such enterprise s business operations continue to qualify for HNTE status. After the first six years, the enterprise would have to go through a new application process in order to renew its HNTE status. As of December 31, 2008, we had received certification of HNTE status for AsiaInfo Technologies, AsiaInfo Technologies (Chengdu), or AICD, and Lenovo Security, which allows for a reduced 15% tax rate starting January 1, 2008. AsiaInfo Technologies was approved as a key software enterprise, and it is eligible for the preferential tax rate of 10% for 2008 and 15% for 2009 and 2010. Lenovo Security was originally granted a 3+3 holiday , and was subject to the applicable tax rate of 0% from 2005 to 2007 and 7.5% from 2008 to 2009, as it maintained its HNTE status. If Lenovo Security continues to maintain its HNTE status in 2010, then it will remain subject to an applicable tax rate of 7.5% in 2010.

Sales of hardware procured in China are subject to a 17% value-added tax. Most of our sales of hardware procured outside of China are made through our U.S. parent company, AsiaInfo Holdings, Inc., and thus are not subject to the value-added tax. We effectively pass value-added tax on hardware sales through to our customers and do not include them in revenues reported in our financial statements. Companies that develop their own software and register the software with the relevant authorities in China are generally entitled to a value-added tax refund. If the net amount of the value-added tax payable exceeds 3% of software sales and software-related services, the excess portion of the value-added tax is refundable immediately. This policy is effective until 2010. The benefit of the rebate of value-added tax is included in our software revenue. Historically, the value-added tax refund is not taxable for income tax purpose as long as the refund is used for research and development activities. However, according to a new tax circular issued by the PRC State Administration of Taxation in January 2009, although the value-added tax refund would remain untaxable, when the refund is used for purchase of or expenses associated with fixed assets, the expenses and depreciation associated with such fixed assets are not deductible for income tax purposes. It is unclear how this new rule will be implemented and in the absence of any specific guidance, we are treating the value-added tax refund as a taxable item for income tax purposes going forward.

Our PRC subsidiaries and VIEs are subject to business tax at the rate of 3% and 5%, respectively, on certain types of service revenues, which are presented in our income statement net of business tax incurred. Business taxes deducted from revenues during the six-month periods ended June 30, 2009 and 2008 were $3.0 million and $1.9 million, respectively.

We are also subject to U.S. income taxes on revenues generated in the United States, including revenues from our limited hardware procurement activities through our U.S. parent company, AsiaInfo Holdings, Inc., and interest income earned in the United States.

Foreign Exchange

A majority of our revenues and expenses relating to the hardware, software and service components of our business are denominated in Renminbi, or RMB. The value of our shares will be affected by the foreign exchange rate between U.S. dollars and RMB because the value of our business is effectively denominated in RMB, while our shares are traded in U.S. dollars. Furthermore, an increase in the value of the RMB may require us to exchange more U.S. dollars into RMB in order to meet the working capital requirements of our subsidiaries in China. Depreciation of the value of the U.S. dollar will also reduce the value of the cash we hold in U.S. dollars, which we may use for purposes of future acquisitions or other business expansion. We actively monitor our exposure to these risks and adjust our cash position in the RMB and the U.S. dollar when we believe such adjustments will reduce our foreign exchange risks. For example, in February 2004 we exchanged approximately $28.0 million cash from U.S. dollars to RMB in order to address concerns regarding a possible increase in the relative value of the RMB. We did not engage in any significant foreign exchange transactions in the three-month period ended June 30, 2009.

As of June 30, 2009, approximately 59.3%, or $112.2 million of our cash, cash equivalents and restricted cash were RMB-denominated and approximately 40.7%, or $77.1 million, were U.S. dollar-denominated. Pursuant to the rate of exchange quoted by People s Bank of China as of June 30, 2009, the exchange rate between the U.S. dollar and the RMB was US$1.00 = RMB6.8319, compared to the rate of US$1.00=RMB6.8591 as of June 30, 2008.

Critical Accounting Policies

We prepare our consolidated financial statements in accordance with US GAAP. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amount of revenues and expenses during the reporting period. On an on-going basis, we evaluate our estimates and judgments, including those related to revenues and cost of revenues under customer contracts, warranty obligations, bad debts, inventories, short-term investments, long-term investments, long-lived assets, income taxes, goodwill and other intangible assets, stock options, and litigation. We base our estimates and judgments on historical experience and on various other factors that we believe are reasonable. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect the more significant judgments and estimates used in the preparation of our consolidated financial statements.

Revenue recognition. Our revenue is derived from three primary sources: (i) software license and related services, including assistance in implementation, customization and integration, post-contract customer support, or PCS, training and consulting; (ii) professional services for systems design, planning, consulting, and system integration; and (iii) the procurement of hardware on behalf of our customers.

Revenues from customer orders requiring significant production, modifications, or customization of the software are recognized over the service period based on the percentage of completion method as prescribed by AICPA Statement of Position No. 81-1, or SOP 81-1, Accounting for Performance of Construction-Type and Certain Product-Type Contracts. Software arrangements with significant production, modifications, or customization are sold with bundled PCS services. Because PCS services have never been sold separately in these arrangements, they do not have stand-alone fair value or vendor specific objective evidence of fair value. The percentage of completion method of revenue recognition is therefore applied to the period from the start of the significant production, modifications, or customization through the last element delivered, which is typically the end of the bundled PCS service period. Revisions in estimated contract costs are made in the period in which the circumstances requiring the revision become known. Provisions, if any, are made currently for anticipated losses on uncompleted contracts.

For software contracts that do not involve significant implementation or customization, license fees are recorded when there is persuasive evidence of an arrangement, the fee is fixed or determinable, collection is probable, and the related products or services are delivered as prescribed by AICPA Statement of Position No. 97-2, or SOP 97-2, Software Revenue Recognition.

The information security products sold by our Lenovo-AsiaInfo division are accounted for under SOP 97-2 because the related software is considered to be more than incidental and is essential to the functionality of the related equipment. These information security products are sold bundled with PCS services over a term of one, two or three years.

For contracts entered into before December 31, 2008, we recognized the total arrangement fee for the information security products as revenue upon delivery assuming all other revenue recognition criteria were met regardless of whether the PCS services terms are one, two or three years because (a) PCS services primarily included telephone and online support, (b) PCS services were substantially provided within the first year of the arrangement term, (c) the costs of providing PCS services had historically been insignificant and were expected to be insignificant in the future, and (d) PCS services did not include upgrades or enhancements. PCS services provided beyond the first year of the service term had historically been negligible. We accrued the estimated costs of providing PCS services upon delivery of the Lenovo-AsiaInfo information security software products.

For contracts entered into after January 1, 2009, we extended PCS services terms so that the PCS services terms include unspecified upgrades. In addition, we have established the vendor-specific objective evidence of fair value of the PCS services. Therefore, the security products revenue is now recognized upon delivery and the PCS services revenue is deferred and recognized pro ratably over the PCS services period.

Consulting and other professional services revenues are recognized when the services are performed. Sales of third-party hardware, if not bundled with other arrangements, are recognized when delivered if all other revenue recognition criteria are met. Costs associated with revenues are recognized when incurred.

Revenue recognized in excess of billings is recorded as unbilled receivables and is included in trade accounts receivable. Amounts billed but not yet collected are recorded as billed receivables and are included in trade accounts receivable. All billed and unbilled amounts are expected to be collected within one year. Billings for installation and customization services are rendered based on agreed upon milestones specified in customer contracts. Billings in excess of revenues recognized are recorded as deferred revenue.

Income taxes. Deferred income taxes are recognized for temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements, net operating loss carry forwards and credits, by applying statutory tax rates applicable to future years. According to the new EIT Law, the transitional rules and relevant regulations, the eligible tax rate for AsiaInfo Technologies is 10% for 2008 and 15% for 2009 and 2010; the eligible tax rate for AICD is 15% for 2008 to 2010, and the eligible rate for Lenovo Security is 7.5% for 2008 to 2010. Unless otherwise specified, our other Chinese subsidiaries and VIEs are subject to the statutory tax rate of 25%.

We record a valuation allowance to reduce our deferred tax assets to the amount that we believe is more likely than not to be realized. In the event we were to determine that we would be able to realize our deferred tax assets in the future in excess of their recorded amount, an adjustment to the deferred tax asset would increase income in the period such determination was made. Likewise, should we determine that we would not be able to realize all or part of our net deferred tax assets in the future, an adjustment to the valuation allowance would be charged to income in the period such change occurred.

On January 1, 2007, we adopted FASB Interpretation No. 48, or FIN 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109. Under FIN 48, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority based solely on technical merits of the associated tax position. Interest and penalties on income taxes will be classified as a component of the provisions for income taxes.

Goodwill. The excess of the purchase price over the fair value of net assets acquired is recorded on the consolidated balance sheet as goodwill. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired. We perform our annual goodwill impairment test on October 1 of each fiscal year for all reporting units. Goodwill is tested following a two-step process. The first step compares the fair value of each reporting unit to its carrying amount, including goodwill. If the fair value of each reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step will not be required. If the carrying amount of a reporting unit exceeds its fair value, the second step compares the implied fair value of goodwill to the carrying value of a reporting unit s goodwill. The implied fair value of goodwill is determined in a manner similar to accounting for a business combination with the allocation of the assessed fair value determined in the first step to the assets and liabilities of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized for any excess in the carrying value of goodwill over the implied fair value of goodwill. We recognized no impairment loss on goodwill in the second quarter of 2009 and 2008.

Consolidated Results of Operations

Revenues. Gross revenues were $58.6 million for the three-month period ended June 30, 2009, representing a 39.3% increase over the year ago period and a 14.9% increase sequentially. Gross revenues for the six-month period ended June 30, 2009 were $109.5 million, which was a year-over-year increase of 42.1%. The year-over-year and sequential increases in gross revenue were primarily driven by strong sales growth among our top three major telecommunications customers: China Mobile, China Unicom, and China Telecom.

Software products and solutions revenue was $47.2 million for the three-month periods ended June 30, 2009, representing an increase of 57.1% over the comparable periods in 2008 and a 11.1% sequential increase. Software products and solutions revenue was $89.6 million for the six-month periods ended June 30, 2009, which was a year-over-year increase of 56.6%. The overall year-over-year and sequential increases in software products and solutions revenue were mainly due to growth in both our telecommunications software business and our IT security business. Telecommunications software products and solutions revenue for the three-month period ended June 30, 2009 was $41.8 million, representing a year-over-year increase of 61.5% and a sequential increase of 6.1%. Telecommunications software products and solutions revenue for the six-month period ended June 30, 2009 was $81.2 million, representing a year-over-year increase of 61.4%. Those increases were due to strong uptake for our software and service solutions among our top three telecommunications customers, whose demand for our products and services increased after the recent telecommunications industry restructuring in China and the issuance of 3G licenses. Software products and solutions revenue from our IT security business in the three-month period ended June 30, 2009 was $5.4 million, representing a 29.9% year-over-year increase and a 75.9% sequential increase. Software products and solutions revenue from our IT security business in the six-month period ended June 30, 2009 was $8.4 million, representing a 23.5% year-over-year increase. The year-over-year increase reflected our concerted effort to improve operations in this division. The sequential increase was partially due to seasonality, as sales in the Lenovo-AsiaInfo business unit are typically weakest in the first quarter. The sequential increase was also attributable to several significant direct-sales contracts we entered into with the PRC government agencies in the second quarter.

Service revenue was $5.9 million in the three-month period ended June 30, 2009, representing an increase of 40.9% over the comparable period in 2008 and a 18.6% sequential increase. Service revenue was $10.9 million in the six-month period ended June 30, 2009, representing an increase of 44.8% over the comparable period in 2008. The year-over-year and sequential increases were primarily due to increased demand for network integration services and an increase in agency service revenue from our arrangement with IBM, where we act as a sales agent in connection with sales of IBM equipment to certain of our telecommunications customers.

Third-party hardware revenue for the three-month period ended June 30, 2009 was $5.5 million, representing a decrease of 30% year-over-year and an increase of 54.8% sequentially. Third-party hardware revenue for the six-month period ended June 30, 2009 was $9 million, representing a decrease of 27.0% year-over-year. Third-party hardware revenue has been generally decreasing in the past several years as we gradually shifted our focus to our software product solutions business. However, from time to time we offer third-party hardware for certain projects in response to customer requests.

Table of Contents

Our Lenovo-AsiaInfo business unit contributed $5.9 million, approximately 10% of our gross revenue in the three-month period ended June 30, 2009, including a 11.4% contribution to software products and solutions revenue and a 1.0% contribution to service revenue. Overall, gross revenue for the Lenovo-AsiaInfo business unit increased 10.6% over the year-ago period and 53.5% sequentially. Our Lenovo-AsiaInfo business unit contributed $9.7 million, approximately 8.9% of our gross revenue in the six-month period ended June 30, 2009, representing an increase of 17.7% over the year-ago period. Our AsiaInfo Technologies business unit contributed $52.7 million, approximately 90% of our gross revenue in the three-month period ended June 30, 2009. Overall, gross revenue for the AsiaInfo Technologies business unit increased by 43.4% over the year-ago period and 11.8% sequentially. Our AsiaInfo Technologies business unit contributed $99.9 million, approximately 91.2% of our gross revenue in the six-month period ended June 30, 2009, representing an increase of 45.1% over the year-ago period.

During the second quarter, sales to our top three customers, China Mobile, China Unicom and China Telecom, accounted for approximately 90% of our total revenue.

Cost of revenues. Our cost of revenues was $29.8 million in the three-month period ended June 30, 2009, representing an increase of 29.5% over the comparable period in 2008. Cost of revenues in the second quarter increased 27% compared to the preceding quarter. Our cost of revenues was $53.2 million in the six-month period ended June 30, 2009, representing an increase of 32.5% over the comparable period in 2008. These changes in cost of revenues were in line with the changes in total revenues for the same periods.

Gross profit. Our gross profit margin in the three-month period ended June 30, 2009 was 49.0%, compared to 45.0% in the same period in 2008 and 54% in the preceding quarter. Our gross profit margin in the six-month period ended June 30, 2009 was 51.4%, compared to 47.9% in the same period in 2008. The year-over-year increase in gross margin reflected an increase in revenues from higher-margin software solutions and services and a decrease in revenue from lower-margin, third-party hardware sales. The sequential decrease was largely the result of increased share-based compensation expenses related to the performance stock unit awards granted to certain of our key employees on March 16, 2009.

Operating expenses. Our operating expenses in the second quarter of 2009 were $22.4 million, representing an increase of 44.4% over the comparable period in 2008 and a 4.9% sequential increase. Our operating expenses in the first half of 2009 were $43.7 million, representing an increase of 42.5% over the comparable period in 2008. The increases were due to increased sales and marketing, research and development, and general administrative expenses, discussed below.

Sales and marketing expenses were $9.9 million for the second quarter of 2009, representing an increase of 20.9% over the comparable period in 2008 and a 5.8% sequential decrease. Sales and marketing expenses were $20.5 million for the first half of 2009, representing an increase of 27.1% over the comparable period in 2008. The year-over-year increases were mainly due to higher sales commission expenses incurred in securing new customer contracts, while the sequential decrease was due to concerted efforts to control sales expenses.

General and administrative expenses were $3.7 million for the second quarter of 2009, representing an increase of 62.5% over the comparable period in 2008 and a 2.4% sequential increase. General and administrative expenses were $7.2 million for the first half of 2009, representing an increase of 48.6% over the comparable period in 2008. The year-over-year and sequential increases were largely the result of increased share-based compensation expenses related to the performance stock unit awards discussed above.

Research and development expenses were $8.8 million for the second quarter of 2009, representing an increase of 74.8% over the comparable period in 2008 and a 21.9% sequential increase. Research and development expenses were $16.0 million for the first half of 2009, representing an increase of 65.2% over the comparable period in 2008. The increases in research and development expenses mainly reflect an increase in headcount, which is in line with the our strategy of continuing to invest in our research and development to take advantage of current and future market opportunities.

Total other income, net. Total other income, including interest income, dividend income, gain from sales of short-term investments, and other (expense) income, net, in the second quarter of 2009 was $1.8 million, representing a decrease of 46.0% over the comparable period in 2008 and an increase of 127.5% over the preceding quarter. Total other income in the first half of 2009 was $2.5 million, representing a decrease of 54.8% over the comparable period in 2008. The year-over-year decrease was largely the result of lower investment gains, as well as lower interest rates in the second quarter of 2009, which resulted in lower interest income. The sequential increase was the result of the sale of certain short-term investments in April 2009.

Income from continuing operations. Income from continuing operations was $7.2 million for the second quarter of 2009, representing an increase of 38.0% over the comparable period in 2008 and an increase of 24.5% sequentially. Income from continuing operations was $13.0 million for the first half of 2009, representing an increase of 36.7% over the comparable period in 2008.

Net income attributable to AsiaInfo Holdings, Inc. Net income attributable to AsiaInfo Holdings, Inc. for the second quarter of 2009 was $7.2 million, or $0.16 per basic share, compared to $5.2 million, or $0.12 per basic share, for the year-ago period, and $5.8 million, or $0.13 per basic share, for the previous quarter. Net income attributable to AsiaInfo Holdings, Inc. for the first half of 2009 was $13.0 million, or $0.30 per basic share, compared to $10.5 million, or $0.23 per basic share, for the year-ago period.

Liquidity and Capital Resources

Our capital requirements are primarily working capital requirements related to hardware sales and costs associated with the expansion of our business, such as research and development and sales and marketing expenses. We recognize hardware costs in full upon delivery of the hardware to our customers. In order to minimize our working capital requirements, we generally obtain from our hardware vendors payment terms that are timed to permit us to receive payment from our customers for the hardware before our payments to hardware vendors are due. With respect to our billing cycle, we generally require our customers to pay 80% to 90% of the invoice value of the hardware upon delivery. We typically place orders for hardware against back-to-back orders from customers and seek favorable payment terms from hardware vendors. However, we sometimes obtain less favorable payment terms from our customers, thereby increasing our working capital requirements. In addition to this careful management of our billing cycle, we have also historically financed working capital and other financing requirements through private placements of equity securities, our initial public offering in 2000 and, to a limited extent, bank loans.

Table of Contents

Our net cash used in operating activities for the three-month period ended June 30, 2009 was $0.3 million. This was primarily attributable to our net income of $7.2 million, adjusted by a net non-cash related expenses of $3.8 million and a net increase in the components of our working capital of $11.3 million.

Our accounts receivable balance as of June 30, 2009 was $103.2 million, consisting of $49.5 million in billed receivables and $53.7 million in unbilled receivables. Our billed receivables are recorded based on agreed-upon milestones included in our customer contracts. Our unbilled receivables are based on the revenues that we have booked through the percentage completion method, but for which we have not yet billed the customer. The IBM Arrangement related accounts receivable balance as of June 30, 2009 was approximately $38.9 million. Our day s sales outstanding as of June 30, 2009 were 96 days, as compared to last quarter s 100 days. When calculating our day s sales outstanding, we use the net accounts receivable balance for the IBM Arrangement where we act as a sales agent and record revenue on a net basis.

Our accounts payable balance as of June 30, 2009 was approximately $54.3 million, compared to $13.8 million as of December 31, 2008. As of June 30, 2009, our accounts payable balance related to our sales agency arrangement with IBM was approximately $39.4 million under which we are contractually obligated to pay our vendor only when China Mobile pays us.

Our net cash used for investing activities for the three-month period ended June 30, 2009 was $5.1 million. This was primarily due to purchase of short-term investments of $10.6 million which was partially offset by the proceeds received from our sale of available-for-sale securities of $6.2 million.

Our net cash generated from financing activities for the three-month period ended June 30, 2009 was $9.5 million. This was primarily from proceeds we received from the exercise of stock options.

As of June 30, 2009, we had cash and cash equivalents and restricted cash totaling $189.3 million and short-term investments totaling $35.4 million.

In April 2009, we, through our majority-owned subsidiary Shanghai Xinjia Information and Technology Co., Ltd., acquired certain operating assets and liabilities of Shanghai Huanyou Information Consultation Co. Ltd., a PRC based provider of value-added telecommunications services, for a cash consideration of $658,000. Goodwill acquired through this acquisition was $410,000. We believe that the transaction furthers our ongoing strategy of expanding our market-leading telecommunications software solutions business in China.

As of June 30, 2009, we had total short-term credit facilities of $34.6 million for working capital purposes, expiring by March 2010, which were secured by bank deposits of $11.0 million. As of June 30, 2009, unused short-term credit facilities were $31.1 million and used facilities totaled $3.5 million. The used facilities were pledged as security for issuing standby letters of credit and trade notes payable to hardware suppliers and customers. Additional bank deposits of $0.9 million were used for issuing standby letters of credit and bank acceptance drafts as of June 30, 2009. Bank deposits pledged as security for these credit facilities totaled $11.9 million as of June 30, 2009 and are presented as restricted cash in our consolidated balance sheets.

We anticipate that our available funds and cash flows generated from operations will be sufficient to meet our anticipated needs for working capital, capital expenditures and business expansion through 2009. We may need to raise additional funds in the future, however, in order to fund acquisitions, develop new or enhanced services or products, respond to competitive pressures to compete successfully for larger projects involving higher levels of hardware purchases, or if our business otherwise grows more rapidly than we currently predict. We anticipate that we would raise additional funds, if necessary, through new issuances of shares of our equity securities in one or more public offerings or private placements, or through credit facilities extended by lending institutions.

In the event that we decide to pay dividends to our stockholders, our ability to pay dividends will depend in part on our ability to receive dividends from our operating subsidiaries in China. Foreign exchange and other regulations in China may restrict our ability to distribute retained earnings from our operating subsidiaries in China or convert those payments from RMB into foreign currencies.

Off-Balance Sheet Arrangements

As of June 30, 2009, we had short-term credit facilities for working capital purposes totaling $34.6 million, expiring by March 2010, of which $3.5 million had been used for issuing standby letters of credit and trade notes payable to hardware suppliers and customers. Unused short-term credit facilities were $31.1 million.

Accounting Pronouncements

On June 12, 2009, the FASB issued Statement of Financial Accounting Standards No. 167, Amendments to FASB Interpretation No. 46(R) (SFAS 167). SFAS 167 is a revision to FIN 46(R) and changes how a company determines whether an entity should be consolidated when such entity is insufficiently capitalized or is not controlled by the company through voting (or similar rights). The determination of whether a company is required to consolidate an entity is based on, among other things, the entity s purpose and design and the company s ability to direct the activities of the entity that most significantly impact the entity s economic performance. SFAS 167 retains the scope of FIN 46(R) but added the entities previously considered qualifying special purpose entities, or QSPEs, since these entities are eliminated from the exemption from consolidation pursuant to SFAS 166. SFAS 167 is effective as of the beginning of the first fiscal year that begins after November 15, 2009. We do not expect the adoption of SFAS 167 to have a significant effect on our consolidated financial position or results of operations.

Table of Contents

At its July 1, 2009 meeting, the FASB ratified the consensus reached on EITF Issue No.09-1 Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing (EITF 09-1). EITF 09-1 applies to share lending arrangements with an entity s own shares when executed in contemplation of a convertible debt offering or other financing. The share lending arrangement is required to be measured at fair value and recognized as an issuance cost associated with the convertible debt offering or other financing. If counterparty default is probable, then the share lender is required to recognize an expense equal to the then fair value of the unreturned shares, net of the fair value of probable recoveries. Entities will be required to apply this new consensus in periods beginning on or after June 15, 2009, for share lending arrangements entered into in those periods. We do not expect the adoption of EITF 09-1 to have a significant effect on our consolidated financial position or results of operations

For information concerning certain risks that may affect our operating results and the value of our common stock, please see Item 1A. Risk Factors in Part II Other Information.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to interest rate risk primarily associated with our cash and short-term investments. To date, we have not entered into any types of derivatives to hedge against interest-rate changes. There have been no significant changes in our exposure to changes in interest rates for the quarter ended June 30, 2009. Our exposure to interest rate changes is limited as we do not have any material borrowings.

We are exposed to exchange rate risk in connection with the relative value of the U.S. dollar and the RMB. Substantially all of our revenues and expenses relating to the service and software components of our business are denominated in RMB. As of June 30, 2009, approximately 59.3%, or $112.2 million of our cash, cash equivalent and restricted cash were RMB-denominated and approximately 40.7%, or $77.1 million, were U.S. dollar-denominated. As of that date, the rate of exchange quoted by the People s Bank of China was US$1.00 = RMB6.8319. If the exchange rate were to increase by 10% to US$1.00 = RMB7.5151, our net assets would potentially decrease by $16.2 million. If the exchange rate were to decrease by 10% to US$1.00 = RMB6.1487, our net assets would potentially increase by $19.8 million**.**

The value of our shares may be affected by the foreign exchange rate between U.S. dollars and RMB because the value of our business is effectively denominated in RMB, while our shares are traded in U.S. dollars. Furthermore, an increase in the value of the RMB may require us to exchange more U.S. dollars into RMB to meet the working capital requirements of our subsidiaries and VIEs in China. Depreciation of the value of the U.S. dollar will also reduce the value of the cash we hold in U.S. dollars, which we may use for purposes of future acquisitions or business expansion. We actively monitor our exposure to these risks and adjust our cash position in the RMB and the U.S. dollar when we believe such adjustments will reduce our foreign exchange risk. For example, in February 2004 we exchanged approximately $28 million cash in US dollars into RMB in anticipation of increases in the value of the RMB. We did not engage in any significant foreign exchange transactions during the three-month period ended June 30, 2009.

As in any other business, we are subject to the risk of macroeconomic changes such as recessions and inflation.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rule 13a-15 under the Exchange Act, as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective.

Changes in Internal Control over Financial Reporting

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2009, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

27

Table of Contents

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On December 4, 2001, a securities class action case was filed in New York City against us, certain of our officers and directors and the underwriters of our initial public offering, or IPO. The lawsuit alleged violations of the US federal securities laws and was docketed in the United States District Court for the Southern District of New York as Hassan v. AsiaInfo Holdings, Inc., et al. The lawsuit alleged, among other things, that the underwriters of our IPO improperly required their customers to pay the underwriters excessive commissions and to agree to buy additional shares of our common stock in the aftermarket as conditions of their purchasing shares in our IPO. The lawsuit further claimed that the alleged practices of the underwriters should have been disclosed in our IPO prospectus and registration statement. The suit seeks rescission of the plaintiffs alleged purchases of our common stock as well as unspecified damages. In addition to the case against us, various other plaintiffs have filed approximately 1,000 other, substantially similar class action cases, or the IPO Allocation Cases, against approximately 300 other publicly traded companies and their IPO underwriters in New York City, which along with the case against us, have all been transferred to a single federal district judge for purposes of case management.

In April of 2009, we and most of the other issuer defendants in the IPO Allocation Cases reached a definitive agreement with the plaintiffs and the underwriter defendants to settle the IPO Allocation Cases. The agreement was filed with the court on April 2, 2009 and preliminarily approved on June 10, 2009. The agreement remains subject to final approval by the court. If the settlement is approved, we expect any damages payable to the plaintiffs to be fully funded by our directors and officers liability insurance policies. If the litigation proceeds, we intend to continue to defend the litigation vigorously. Moreover, if the litigation proceeds, we believe that the underwriters may have an obligation to indemnify us for the legal fees and other costs of defending this suit and that our directors and officers liability insurance policies would also cover the defense and potential exposure in the suit.

In addition, we received a letter dated July 30, 2007 from a putative stockholder demanding that we investigate and prosecute a claim for alleged short-swing trading in violation of Section 16(b) of the Exchange Act by the underwriters of our IPO and certain of our unidentified directors, officers and stockholders. On October 9, 2007, the putative stockholder commenced a civil lawsuit in the U.S. District Court for the Western District of Washington against Morgan Stanley and Deutsche Bank, two of the lead underwriters of our IPO, alleging violations of Section 16(b) of the Exchange Act. The complaint alleges that the combined number of shares of our common stock beneficially owned by the lead underwriters and certain unnamed officers, directors and principal stockholders exceeded ten percent of our outstanding common stock from the date of our IPO on March 3, 2000, through at least March 2, 2001. It further alleges that those entities and individuals were thus subject to the reporting requirements of Section 16(a) and the short-swing trading prohibition of Section 16(b), and failed to comply with those provisions. The complaint seeks to recover from the lead underwriters any short-swing profits obtained by them in violation of Section 16(b). None of our directors, officers or stockholders is named as defendants in this action, although we are named as a nominal defendant. On July 25, 2008, we filed a joint motion to dismiss, with several other issuers who are also named as nominal defendants in the action. On March 12, 2009, the court granted our motion, dismissing the complaint without prejudice on the ground that the plaintiff failed to make an adequate demand to us prior to filing her complaint. Plaintiff filed a Notice of Appeal on April 10, 2009.

We intend to continue to defend vigorously the two litigation matters described above. While we cannot guarantee the outcome of these proceedings, we believe that the final results of these lawsuits will have no material effect on our consolidated financial condition, results of operations, or cash flows.

During the fiscal quarter ended June 30, 2009, we did not have any other material legal proceedings brought against us. No further material developments occurred in connection with any previously reported legal proceedings against us during the last fiscal quarter.

ITEM 1A. RISK FACTORS

Certain Risks That May Affect Our Operating Results and Our Common Stock

In addition to the other information in this report, the following factors should be considered in evaluating our business and our future prospects:

Our customer base is concentrated and the loss of one or more of our customers could cause our business to suffer significantly.

We have derived, and believe that we will continue to derive, a significant portion of our revenues from a limited number of large customers in the telecommunications industry in China, such as China Mobile, China Telecom and China Unicom. China Mobile accounted for 60% of our revenues in 2008 and 58% of our revenues in 2007. The loss, cancellation or deferral of any large contract would have a material adverse effect on our revenues, and consequently our profits. Despite our entering the IT security products and services market following the acquisition of Lenovo s IT service segment in 2004, the revenue expected to be generated by customers outside the telecommunications industry is still limited compared to our overall revenues. Moreover, we cannot provide any assurance that a material proportion of our revenues will be derived from other customers in the future.

Table of Contents

The growth of our business is dependent on government telecommunications infrastructure and budgetary policies, particularly the allocation of funds to sustain the growth of the telecommunications industry in China.

Our telecommunications customers are directly or indirectly owned or controlled by the government of China. Accordingly, their business strategies, capital expenditure budgets and spending plans are largely decided in accordance with government policies, which, in turn, are determined on a centralized basis at the highest level by the National Development and Reform Commission of China. As a result, the growth of our business is heavily dependent on government policies for telecommunications infrastructure. Insufficient government allocation of funds to sustain the growth of China s telecommunications industries in the future could reduce the demand for our products and services and have a material adverse effect on our ability to grow our business.

The Chinese economic slow-down may negatively impact our operating results.

The Chinese economy has recently experienced a slowing of its growth rate. A number of factors have contributed to this slow-down, including appreciation of the Renminbi, the currency of China, or RMB, which has adversely affected China s exports. In addition, the slow-down has been exacerbated by the recent global crisis in the financial services and credit markets, which has resulted in significant volatility and dislocation in the global capital markets. It is uncertain how long the global crisis in the financial services and credit markets will continue and how much adverse impact it will have on the global economy in general or the Chinese economy in particular. Slowing economic growth in China could result in slowing growth for China s major telecommunications carriers, which are our largest customers, as well as slowing growth for enterprises and government entities that buy our IT security software and services. Any such adverse conditions for our customers could reduce their demand for our software and services and therefore reduce our revenues.

Further restructuring of China s telecommunications sector may have an adverse impact on our business prospects and results of operations.

Historically, China s telecommunications sector has been subject to a number of state-mandated restructurings. For example, in 2002 China Telecom was split geographically into a northern division (comprising 10 provinces) and a southern division (comprising 21 provinces). Under the restructuring, the northern division of China Telecom merged with China Netcom and was renamed China Network Communications Group Corporation, or China Netcom Group, while the southern division continued to use the China Telecom name. As a result of the restructuring, new orders for telecommunications infrastructure expansion and improvement projects decreased, which adversely affected our revenue. Any similar restructurings of this nature could cause our operating results to vary unexpectedly from quarter to quarter in the future.

In May 2008, China announced a new restructuring plan for the country s telecommunications operators. This restructuring plan reorganized the operations of Chinese telecommunications carriers, creating three major operators that have both mobile and fixed-line services. It is the Chinese government s intention to enhance the competitiveness of local telecommunications operators and clear the way for 3G licenses, which were released after the completion of this restructuring. Such restructuring could disrupt, slow down or otherwise materially affect our customers capital expenditures on telecommunications infrastructure and improvement projects and, therefore, our revenues. Additionally, the competitive situation in the wireless communications market in China may be altered, or the resulting entities may change suppliers or sourcing policies. If China Mobile or any of our other large customers decides to significantly change its procurement methods for telecommunications software and services, reduces or eliminates the purchase of our software and services or becomes unable or refuses to pay for our software and services, our revenues would decline significantly.

Any future acquisitions or investments we make may expose us to potential risks and have an adverse effect on our ability to manage our business.

Selective acquisitions and strategic investments form part of our strategy to further expand our business. If we are presented with appropriate opportunities that we feel will enhance our revenue growth, operations and profitability, we may acquire additional businesses, services or products that are complementary to our core business. Such acquisitions could result in the use of significant amounts of cash and/or dilutive issuances of our common stock. Such acquisitions also involve other significant risks. For example, our integration of such acquired entities and/or operations into our business may not be successful and may not enable us to expand into new business platforms as well as we expect. This would significantly affect the expected benefits of these acquisitions. Moreover, the integration of new businesses into our operations has required significant attention from our management. Future acquisitions will also likely present similar challenges.

Future acquisitions or strategic investments may also expose us to other potential risks, including risks associated with unforeseen or hidden liabilities, the diversion of resources from our existing businesses and potential loss, or harm to, relationships with employees and clients as a result of our integration of new businesses. In addition, we cannot be sure that we will be able to realize the benefits we anticipate from acquiring any business, services and products, or that we will not incur costs, including those relating to intangible assets or goodwill, in excess of our projected costs for these transactions. The occurrence of any of these events could have a material and adverse effect on our ability to manage our business, our financial condition and our results of operations.

The long and variable sales cycles for our software and services can cause our revenues and operating results to vary significantly from period to period and may adversely affect the trading price of our common stock.

Our revenues and operating results will vary significantly from quarter to quarter due to a number of factors, many of which are outside of our control and any of which may cause our stock price to fluctuate. A customer s decision to purchase our software and services involves a significant commitment of its resources and extended evaluation. As a result, our sales cycle tends to be lengthy. We spend considerable time and expense educating and providing information to prospective customers about features and applications of our software and services. Because our major customers often operate large and complex networks, they usually expand their networks in large increments on a periodic basis. The combination of these factors can cause our revenues and results of operations to vary significantly and unexpectedly from quarter to quarter.

Table of Contents

A large part of the contract amount of our projects sometimes relates to hardware procurement. Since we recognize most of the revenues relating to hardware plus a portion of services and software revenues at the time of hardware delivery, the timing of hardware delivery can cause our quarterly gross revenues to fluctuate significantly. Due to the foregoing factors, we believe that quarter to quarter comparisons of our results of operations may not be a good indication of our future performance and should not be overly relied upon. It is likely that our results of operations in some periods may be below the expectations of public market analysts and investors. In this event, the price of our common stock will probably decline, perhaps significantly more in percentage terms than any corresponding decline in our operating results.

Our working capital requirements may increase significantly.

We typically purchase hardware for our customers as part of our turn-key total solutions services. We generally require our customers to pay 80% to 90% of the invoice value of the hardware upon delivery. We typically place orders for hardware against back-to-back orders from customers and seek favourable payment terms from hardware vendors. This policy has historically minimized our working capital requirements. However, for certain large and strategically important projects, we have agreed to payment of less than 80% to 90% of the invoice value of the hardware upon delivery in order to maintain competitiveness. Wider adoption of less favourable payment terms or delays in hardware deliveries could cause our working capital needs to increase significantly.

We have sustained losses in prior years and may incur slower earnings growth, earnings declines or net losses in the future.

Although we had net income in 2004, 2006, 2007 and 2008, we sustained net losses in 2005. There are no assurances that we can sustain profitability or avoid net losses in the future. We continue to expect that certain of our operating expenses will increase as our business grows. The level of these expenses will be largely based on anticipated organizational growth and revenue trends and a high percentage of those expenses, particularly compensation expenses, will be fixed. As a result, any delays in expanding sales volume and generating revenue could result in substantial operating losses or slower earnings growth or earnings declines.

Our high level of fixed costs, as well as increased competition in the software market, could result in reduced operating margins.

We maintain a relatively stable work force of software and network engineers engaged in all phases of planning and executing projects on behalf of our customers. As a result, our operating costs are relatively fixed from quarter to quarter, regardless of fluctuations in our revenues. Future fluctuations in our revenues could result in decreases in our operating margins. In addition, enhanced competition in the software market and other markets in which we operate could result in reduced prices, which, together with our relatively fixed operating costs, could also result in reduced operating margins. Moreover, our operating margins may decline as a result of the strong bargaining power of our customers, general economic conditions or the restructuring of the telecommunications sector in China.

China s laws and regulations currently prohibit foreign-invested companies from engaging in systems integration businesses involving state secrets, which is part of the IT services business we acquired from Lenovo in 2004. China s laws and regulations also restrict certain foreign-invested companies from participating in the value-added telecommunications, or VATS, business. Substantial uncertainties exist with respect to our contractual arrangements with our affiliates engaged in these businesses, due to uncertainties regarding the interpretation and application of current and future China laws and regulations.

In 2001, the State Secrecy Bureau of China promulgated the Administrative Measures for Qualification of Computer Information Systems Integration Involving State Secrets, which expressly prohibits foreign persons or foreign-invested enterprises from engaging in systems integration businesses involving state secrets, also referred to as restricted businesses . We and our PRC operating subsidiaries in China are considered foreign persons or foreign-invested enterprises under the laws of China and cannot therefore engage in restricted businesses. Many of the IT security services provided by our Lenovo-AsiaInfo division comprise restricted businesses. We operate the restricted businesses primarily through contractual agreements with Lenovo Security Technologies (Beijing), Inc., or Lenovo Security, and Lenovo Computer System and Technology Services Limited, or Lenovo Computer. When we acquired the restricted businesses, we agreed to have Lenovo Security engage in the operation of the restricted businesses upon Lenovo Security s receipt of all requisite business licenses and qualifications, such as the Computer Information System Integration Involving State Secrets Qualification Certificate issued by the State Secrecy Bureau of China for Protection of State Secrets. Lenovo Security has obtained most of these licenses. Certain licenses are subject to annual review and we cannot assure you that Lenovo Security can successfully renew such licenses. Since September, 2006, Lenovo Security has conducted most of our operations related to the restricted businesses and, consequently, generates most of our revenue derived from the restricted businesses.

Lenovo Computer is owned by certain subsidiaries of Lenovo. Lenovo Security is owned by Legend Holdings Limited, the parent company and controlling shareholder of Lenovo, and two of our employees, Mr. Jian Qi, the President and Chief Executive Officer of Lenovo-AsiaInfo division, and Ms. Zheng Wang, our Director of Investments. Mr. Qi and Ms. Wang are citizens of China. We do not currently have any equity interest in either Lenovo Computer or Lenovo Security, but instead enjoy economic benefits and control over these entities substantially similar to equity ownership through contractual arrangements among one of our wholly-owned subsidiaries, these affiliated entities and their respective shareholders. Consistent with the provisions of Financial Accounting Standard Board FASB Interpretation No. 46 (revised), Consolidation of Variable Interest Entities an Interpretation of ARB No. 51, we consolidated the operating results of Lenovo Computer and Lenovo Security with our operating results.

Table of Contents

At the closing of our acquisition of Lenovo s IT services business, our PRC legal counsel who represented us in the transaction, T&C Law Firm, and PRC legal counsel to Lenovo Group, Tian Yuan Law Firm, each delivered legal opinions to the effect that our ownership structure of Lenovo Computer and Lenovo Security, and the contractual arrangements among Lenovo-AsiaInfo, these affiliated entities and their respective shareholders, were in compliance with all existing PRC laws and regulations. There are, however, substantial uncertainties regarding the interpretation and application of current or future PRC laws and regulations, including regulations governing the validity and enforcement of such contractual arrangements. Accordingly, we cannot assure you that PRC government authorities will not ultimately take a view contrary to the opinion of our and Lenovo s PRC legal counsel.

Like the IT security business in China, many aspects of the telecommunications services industry, such as VATS, are also restricted from foreign ownership in most circumstances. In September 2004 we entered into contractual arrangements with Star VATS, a domestic company owned by certain of our employees who are citizens of China, which has been established to engage in the VATS business in China. Star VATS is in the process of developing VATS products and services that we hope to offer in China. We anticipate that if we successfully launch our VATS products and services, all of our business related to such products and services will be conducted through Star VATS. Star VATS will generate any revenue relating to such business and will make use of the licenses and approvals that are essential to such business. We do not have any equity interest in Star VATS, but instead have the right to enjoy economic benefits similar to equity ownership through our contractual arrangements with Star VATS and its shareholders. In the opinion of our PRC legal counsel who represented us in the transaction, T&C Law Firm, delivered at the time Star VATS was established, the contractual arrangements among us, Star VATS, and the shareholders of Star VATS were in compliance with all existing PRC laws and regulations. There are, however, substantial uncertainties regarding the interpretation and application of current and future PRC laws and regulations, including regulations governing the validity and enforcement of such contractual arrangements. Accordingly, we cannot assure you that China government authorities will not ultimately take a view contrary to the opinion of our PRC legal counsel.

In addition, as part of the contractual arrangements described above, the shareholders of Lenovo Computer, Lenovo Security and Star VATS agreed to pledge their respective shares in those entities to certain of our subsidiaries. Pursuant to a regulation in China known as the Provisions for Changes of Investors Equity in Foreign Invested Enterprises, effective May 28, 1997, a pledge of the equity interests of a foreign-invested enterprise will only be effective after obtaining approval from and registering with the relevant governmental authorities. Furthermore, under the PRC Property Rights Law, effective October 1, 2007, a pledge is created only after registration with the local branch of the Administration for Industry and Commerce in China. The pledges of the equity interests in Lenovo Computer, a foreign-invested company, have not yet been approved by or registered with the relevant governmental authorities in China. Lenovo Computer intends, however, to take the necessary steps to comply with the requirements described above. In addition, the pledges of the equity interests in Lenovo Security have not been registered with the relevant governmental authorities in China because the registration procedures were only recently announced. Lenovo Security is currently in the process of registering such pledges. The pledges of the equity interests in Star VATS have recently been registered with the relevant governmental authorities in China. Before compliance with the approval and registration requirements described above, we cannot assure you that these pledges will be effective or deemed created by the relevant governmental authorities.

If we or any of our contractual arrangements with Lenovo Computer, Lenovo Security and Star VATS are found to be in violation of any existing or future PRC laws or regulations concerning the systems integration business involving state secrets or the VATS businesses, the relevant PRC regulatory authorities would have broad discretion in dealing with such violations, including:

- revoking the business licenses of our subsidiaries in China;
- discontinuing or restricting our PRC subsidiaries operations;
- imposing conditions or requirements with which we or our PRC subsidiaries may not be able to comply; or
- requiring us or our PRC subsidiaries to restructure the relevant ownership structure or operations.

The imposition of any of these penalties could have a material adverse effect on our ability to conduct our business.

The principal shareholders and directors of Lenovo Security, Lenovo Computer and Star VATS may have potential conflicts of interest with us, which may adversely affect our business.

We operate the restricted businesses in China primarily through Lenovo Security and Star VATS, which are jointly owned by certain of our employees, and through Lenovo Computer, which is indirectly owned by Lenovo Group Limited, the indirect parent company of one of our stockholders. Conflicts of interests between their duties to us and to Lenovo Security, Lenovo Computer and Star VATS may arise. We cannot assure you that when conflicts of interest arise, any or all of these persons will act in the best interests of our company or that any conflict of interest will be resolved in our favor. In addition, these persons or their heirs or other successors may breach or cause Lenovo Security, Lenovo Computer and Star VATS to breach or refuse to renew the existing contractual arrangements that allow us to effectively control Lenovo Security and Lenovo Computer and Star VATS and to receive economic benefits from them. Other than relying on the duties of loyalty owed to us by the shareholders of Lenovo Security and Star VATS who are also our officers, and the contractual arrangements with the shareholders of Lenovo Security, Lenovo Computer and Star VATS, we currently do not have any measure or policy to address these potential conflicts of interest. In the event of any disputes regarding the contractual arrangements, we would have to rely on legal remedies under PRC law. These remedies may not always be effective, particularly in light of uncertainties in the PRC legal system. If we cannot resolve any conflicts of interest or disputes between us and the shareholders of Lenovo Security, Lenovo Computer and Star VATS, we would have to rely on legal proceedings, the outcome of which may be uncertain and which could be disruptive to our business.

Our contractual arrangements with Lenovo Computer, Lenovo Security and Star VATS may not be as effective in providing operational control as direct ownership of these affiliated entities and may be difficult to enforce.

We rely on contractual arrangements with Lenovo Computer, Lenovo Security and Star VATS to operate our IT security and VATS businesses. These contractual arrangements, which require Lenovo Computer, Lenovo Security and Star VATS to pay service and licensing fees to our subsidiaries in China, are currently the primary means by which we could receive economic benefits from these affiliated companies. In the future, we expect to continue to obtain economic benefits from Lenovo Computer, Lenovo Security and Star VATS through these contractual arrangements. Although we have been advised by our PRC legal counsel that our contractual arrangements with Lenovo Computer, Lenovo Security and Star VATS are valid, binding and enforceable under PRC laws, these contractual arrangements may not be as effective as direct ownership of these affiliated entities. For example, these affiliated entities and their respective shareholders could fail to perform or make payments as required under such contractual arrangements. In such event, we would have to rely on the PRC legal system to enforce these agreements. Any legal proceedings would be uncertain as to outcome and could result in the disruption of our business, damage to our reputation, diversion of our resources and the incurrence of substantial costs.

In addition, in the event we are unable to so extend our contractual arrangements, we may fail to obtain the requisite license to conduct certain IT security and VATS businesses in China and may be required to temporarily suspend these businesses.

Contractual arrangements we have entered into between our subsidiaries and each of Lenovo Computer, Lenovo Security and Star VATS may be subject to scrutiny by China tax authorities, and a finding that we or any of our subsidiaries or any of Lenovo Computer, Lenovo Security and Star VATS owe additional taxes or are ineligible for our preferential tax treatment, or both, could substantially increase our taxes owed, or could materially reduce our profits and the value of your investment.

Under PRC law, arrangements and transactions among related parties may be audited or challenged by the tax authorities in PRC. If any of the transactions between our subsidiaries and each of Lenovo Computer, Lenovo Security and Star VATS are found to not have been entered into on an arm s-length basis, or to result in an unreasonable reduction in tax under PRC law, the tax authorities in China have the authority to disallow our tax savings, adjust the profits and losses of our respective Chinese entities and assess late payment interest and penalties. A finding by the tax authorities in China that we are ineligible for certain tax savings, or that any of our subsidiaries or any of Lenovo Computer, Lenovo Security and Star VATS is ineligible for their preferential tax treatment, could increase our taxes owed and reduce our profits and the value of your investment.

We may not be able to operate the systems integration businesses involving state secrets if we acquire all of the equity interest in Lenovo Computer and Lenovo Security.

PRC laws and regulations currently prohibit foreign persons or foreign-invested enterprises from engaging in systems integration businesses involving state secrets. We and our subsidiaries are considered foreign persons or foreign-invested enterprises under China laws. Unless such prohibition is lifted in the future, we will not be able to operate such business if and when we acquire all of the equity interest in Lenovo Computer and Lenovo Security pursuant to the terms of our contractual arrangements with Lenovo Computer and Lenovo Security and their respective shareholders. The loss of this line of business may materially and adversely affect our business, financial condition and results of operations.

Regulations relating to acquisitions of Chinese companies by foreign entities may limit our ability to acquire Chinese companies and adversely affect the implementation of our acquisition strategy and any failure by our stockholders who are Chinese residents to make or obtain any required registrations pursuant to such regulations may subject us to legal sanctions.

On October 21, 2005, the PRC State Administration of Foreign Exchange, or SAFE, issued a notice, known as Circular 75, which sets forth a regulatory framework for acquisitions of PRC businesses involving offshore companies owned by a PRC residents or passport holders, known as round-trip investments or acquisitions. Among other things, Circular 75 provides that if a round-trip investment in a PRC company by an offshore company controlled by PRC residents occurred prior to the issuance of Circular 75, certain PRC residents were required to submit a registration form to the local SAFE branch to register their ownership interests in the offshore company prior to March 31, 2006. Circular 75 also provides that, prior to establishing or assuming control of an offshore company for the purpose of obtaining financing for that offshore company using the assets or equity interests in an onshore enterprise in the PRC, each PRC resident or passport holder who is an ultimate controller of such offshore company, whether an individual or a legal entity, must complete the overseas investment foreign exchange registration procedures with the relevant local SAFE branch. Such PRC residents must also amend the registration form if there is a material event affecting the offshore company, such as, among other things, a change in share capital, a transfer of shares, or if such company is involved in a merger, acquisition or a spin-off transaction or uses its assets in China to guarantee offshore obligations. In May 2007, SAFE issued guidance to its local branches with respect to the operational process for SAFE registration, known as Circular 106, which standardized registration under Circular 75. In the past, we have acquired a number of assets from, or equity interests in, PRC companies. However, there is substantial uncertainty as to whether we would be considered an offshore company for purposes of Circular 75, and, at present, it is unclear whether Circular 75 requires a company such as ours to register. We have in any event requested our stockholders who are PRC residents to make the necessary applications, filings and amendments as required under Circular 75 and other related regulations. We will attempt to comply, and attempt to ensure that all of our stockholders subject to these rules comply, with the relevant requirements. We cannot, however, assure the compliance of all of our PRC-resident stockholders. Any failure to comply with the relevant requirements could subject us to fines or sanctions imposed by the PRC government, including restrictions on certain of our subsidiaries ability to pay dividends to us and our ability to increase our investment in those subsidiaries.

Table of Contents

As Circular 75, Circular 106 and related regulations are relatively new and it is uncertain how these regulations will be interpreted, implemented or enforced, we cannot predict how these regulations will affect our future acquisition strategies and business operations. For example, if we decide to acquire additional PRC companies, we cannot assure you that we or the owners of such companies will be able to complete the filings and registrations, if any, required by Circular 75, Circular 106 and related regulations. Under Circular 75, failure to comply with the registration procedures set forth thereunder may result in the imposition of restrictions on the foreign exchange activities of the relevant onshore company, including the payment of dividends and other distributions to its offshore parent or affiliate and the capital inflow from the offshore entity, and may also subject relevant PRC residents to penalties under PRC foreign exchange administration regulations. Any such restrictions or penalties may restrict our ability to implement an acquisition strategy and could adversely affect our business and prospects.

In addition, six PRC regulatory authorities, including the PRC Ministry of Commerce and the Chinese Securities Regulatory Commission, or CSRC, jointly promulgated regulations entitled Provisions regarding Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, or the New M&A Rules effective September 8, 2006. The New M&A Rules established additional procedures and requirements that make merger and acquisition activities by foreign investors more time-consuming and complex, including, in some circumstances, advance notice to the Ministry of Commerce of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise. Compliance with the New M&A Rules, and any related approval processes, including obtaining approval from the Ministry of Commerce, may delay or inhibit our ability to complete acquisitions of domestic PRC companies, which could affect our ability to expand our business or maintain our market share.

Furthermore, on August 29, 2008, SAFE issued a notice, known as Circular 142, regulating the conversion by a foreign-invested company of foreign currency into RMB by restricting the uses for the converted RMB. Circular 142 requires that the registered capital of a foreign-invested company denominated in RMB but converted from a foreign currency may only be used pursuant to the purposes set forth in the foreign-invested company s business scope as approved by the applicable governmental authority. Such registered capital may not be used for equity investments within the PRC. In addition, SAFE strengthened its oversight of the flow and use of the registered capital of a foreign-invested company that was denominated in RMB but converted from foreign currency. The use of such registered capital may not be changed without SAFE s approval, and may not in any case be used to repay RMB loans if the proceeds of such loans have not been used. Violations of Circular 142 may result in severe penalties, including significant fines. As a result, Circular 142 may significantly limit our ability to invest in or acquire other PRC companies using the RMB-denominated capital of our PRC subsidiaries.

Asset impairment reviews may result in future write-downs.

Effective January 1, 2002, we adopted SFAS No. 142, which requires us, among other things, to conduct annual reviews of goodwill, and SFAS No. 144, which requires us to test intangible assets for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. In connection with our business acquisitions, we make assumptions regarding estimated future cash flows and other factors to determine the fair value of goodwill and intangible assets. In assessing the related useful lives of those assets, we have to make assumptions regarding their fair value, our recoverability of those assets and our ability to successfully develop and ultimately commercialize acquired technology. If those assumptions change in the future when we conduct our periodic reviews in accordance with applicable accounting standards, we may be required to record impairment charges. For example, we recorded a non-cash impairment charge of $21.2 million as a result of an independent valuation during the fourth quarter of 2005 of the goodwill and acquired intangible assets mainly attributable to our acquisition of Lenovo s IT services business in 2004. It is possible that future reviews will result in further write-downs of goodwill and other intangible assets.

We have recorded a US$4.6 million non-cash impairment charge to net income, and may be required to record additional significant charges to earnings from the declines in fair value of our marketable securities if such declines become other than temporary.

Our short-term investment policy and strategy attempt primarily to preserve capital and meet our liquidity requirements. Our marketable securities are classified as available-for-sale securities in short-term investments and are reported at fair value with net unrealized losses recognized as accumulated other comprehensive income in stockholders equity unless there is a decline in fair value below cost that we consider is other than temporary, in which case the amount of the decline would be recognized as a loss and reflected in our income statement. As of December 31, 2008, we recognized a $4.6 million non-cash impairment charge to net income related to our short-term investments in certain stock funds. We review our short-term investments to determine whether any differences between cost and fair value are other-than-temporary impairment in accordance with FASB Staff Position SFAS 115-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments and SEC Staff Accounting Bulletin Topic 5M, The Meaning of Other-Than-Temporary Impairment of Certain Investments in Debt and Equity Securities. In addition, as of December 31, 2008, we also recognized a $2.0 million impairment on long-term investments, representing the decline in fair value of our 5% equity stake in Hinge Software Company Limited, a Shanghai-based provider of business intelligence software solutions. We review long-term investments for impairment whenever events or changes in circumstances indicate that the carrying value of such investments may no longer be recoverable.

The losses incurred on these short-term and long-term investments are primarily related to the changes in the general global market conditions. If factors arise that would require us to account for additional declines as other than temporary or if we are unable to hold investments until the carrying value of such investments is recovered, we may need to recognize the declines as additional realized losses with a charge to income, which could have a material adverse effect on our financial condition and operating results.

We may be subject to fines and legal sanctions if we or our employees who are PRC citizens fail to comply with recent PRC regulations relating to employee stock options granted by overseas listed companies to PRC citizens.

On March 28, 2007, SAFE issued the Application Procedure for Foreign Exchange Administration for Domestic Individuals Participating in Employee Stock Holding Plans or Stock Option Plans of Overseas Listed Companies , also known as Circular 78. Under Circular 78, PRC individuals who participate in an employee stock option holding plan or a stock option plan of an overseas listed company are required, through a PRC domestic agent or PRC subsidiary of the overseas listed company, to register with SAFE and complete certain other procedures. We and our Chinese employees who have been granted restricted stock units or stock options pursuant to our stock incentive plans are subject to Circular 78 because we are an overseas listed company. However, in practice, significant uncertainties exist with respect to the interpretation and implementation of Circular 78. We intend to submit the application for registration of our employee stock incentive plan as soon as possible. We cannot provide any assurance that we or our Chinese employees will be able to comply with, qualify under, or obtain any registration required by Circular 78. In particular, if we or our Chinese employees fail to comply with the provisions of Circular 78, we or they may be subject to fines and legal sanctions imposed by SAFE or other PRC governmental authorities, which could result in a material and adverse effect to our business operations and employee stock incentive plans.

We are highly dependent on our executive officers.

Each of our executive officers is responsible for an important sector of our operations. Although we believe that we have significant depth at all levels of management, the loss of any of our executive officers services could be detrimental to our operations. We do not have, and do not plan to obtain, key man life insurance on any of our officers.

We face a competitive labor market in China for skilled personnel and therefore are highly dependent on the skills and services of our existing key skilled personnel and our ability to hire additional skilled employees.

Competition for highly skilled software design, engineering and sales and marketing personnel is intense in China. Our failure to attract, assimilate or retain qualified personnel to fulfill our current or future needs could impair our growth. Competition for skilled personnel comes primarily from our local competitors, as well as a wide range of foreign companies active in China, many of which have substantially greater resources than we have. Limitations on our ability to hire and train a sufficient number of personnel at all levels would limit our ability to undertake projects in the future and could cause us to lose market share.

Increases in wages for software design, engineering, sales and marketing and management personnel will increase our net cash outflow and our gross margin and profit margin may decline.

Historically, wages for comparably skilled technical and management personnel in the telecommunications software solutions and IT security products industry in China have been lower than in developed countries, such as in the U.S. or Europe. In recent years, wages in China s software and IT security industry have increased and may continue to increase at faster rates. Wage increases will increase our cost of our products and services of the same quality and increase our cost of operations. As a result, our gross margin and profit margin may decline. In the long term, unless offset by increases in efficiency and productivity of our work force, wage increases may also result in increased prices for our solutions and services, making us potentially less competitive. Increases in wages, including an increase in the cash component of our compensation expenses, will increase our net cash outflow and our gross margin and profit margin may decline.

We extend warranties to our customers that expose us to potential liabilities.

We customarily provide our customers with one to three year warranties, which cover third-party hardware and software products. Although we seek to arrange back-to-back warranties with hardware and software vendors, we have the primary responsibility with respect to their warranties. Our contracts often lack disclaimers or limitations on liability for special, consequential and incidental damages, nor do we typically cap the amounts our customers can recover for damages. In addition, we do not currently purchase any insurance policy with respect to our exposure to warranty claims. The failure of our installed projects to operate properly could give rise to substantial liability for special, consequential or incidental damages, which in turn could materially and adversely affect us.

We sell our services on a fixed-price, fixed-time basis, which exposes us to risks associated with cost overruns and delays.

We sell most of our services on a fixed-price, fixed-time basis. In contracts with our customers, we typically agree to pay late completion fines of up to 5% of the total contract value. In large scale telecommunications infrastructure projects, there are many factors beyond our control which could cause delays or cost overruns. In this event, we would be exposed to cost overruns and liability for late completion fines.

We may become less competitive if we are unable to develop or acquire new products, or enhancements to our existing products, that are marketable on a timely and cost-effective basis.

Our future operating results will depend, to a significant extent, upon our ability to enhance our existing products and services and to introduce new products and services to meet the requirements of our customers in a rapidly developing and evolving market. If we do not enhance our existing products and services or introduce new successful products and services in a timely manner, our products and services may become obsolete, and our revenues and operating results may suffer. Moreover, unexpected technical, operational, distribution or other problems could delay or prevent the introduction of any products or services that we may plan to introduce in the future. We cannot be sure that any of these products or services will achieve widespread market acceptance or generate incremental revenues.

Table of Contents

Our proprietary rights may be inadequately protected and there is a risk of poor enforcement of intellectual property rights in China.

Our success and ability to compete depend substantially upon our intellectual property rights, which we protect through a combination of confidentiality arrangements and copyright, trademark, and patent registrations. We have registered some marks and filed trademark applications for other marks with the United States Patent and Trademark Office, the Trademark Bureau of the State Administration of Industry and Commerce in China and the Trade Marks Registry in Hong Kong. We have also registered copyrights with the State Copyright Bureau in China with respect to certain of our software products, although we have not applied for copyright protection elsewhere (including the U.S.). We have filed some patent applications and have acquired some existing patents in China for certain hardware and software products used or developed in our business. Despite these precautions, the legal regime protecting intellectual property rights in China is weak. Because the Chinese legal system in general and the intellectual property regime in particular, are relatively weak, it is often difficult to enforce intellectual property rights in China. In addition, there are other countries where effective copyright, trademark and trade secret protection may be unavailable or limited.

We enter into confidentiality agreements with most of our employees and consultants, and control access to, and distribution of, our documentation and other licensed information. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our licensed services or technology without authorization, or to develop similar technology independently. Policing unauthorized use of our licensed technology is difficult and there can be no assurance that the steps we take will prevent misappropriation or infringement of our proprietary technology. In addition, litigation may be necessary to enforce our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others, which could result in substantial costs and diversion of our resources.

A portion of our business involves the development and customization of software applications for customers. We generally retain significant ownership or rights to use and market such software for other customer projects, where possible. However, our customers sometimes retain co-ownership and rights to use the applications, processes, and intellectual property so developed. In some cases, we may have no right or only limited rights to reuse or provide these developments to projects involving other customers. To the extent that we are unable to negotiate contracts which permit us to reuse source-codes and methodologies, or to the extent that we have conflicts with our customers regarding our ability to do so, we may be unable to provide similar solutions to our other customers.

We are exposed to certain business and litigation risks with respect to technology rights held by third parties.

We currently license technology from third parties and intend to do so increasingly in the future as we introduce services that require new technology. There can be no assurance that these technology licenses will be available to us on commercially reasonable terms, if at all. Our inability to obtain any of these licenses could delay or compromise our ability to introduce new services. In addition, we may or may allegedly breach the technology rights of others and incur legal expenses and damages, which could be substantial.

Investors may not be able to enforce judgments entered by United States courts against certain of our officers and directors.

We are incorporated in the State of Delaware. However, a majority of our directors and executive officers, and certain of our principal stockholders, live outside of the U.S., principally in Beijing and Hong Kong. As a result, you may not be able to:

- effect service of process upon those persons within the U.S.; or
- enforce against those persons judgments obtained in United States courts, including judgments relating to the federal securities laws of the U.S.

The fact that our business is conducted in both U.S. dollars and RMB may subject us to currency exchange rate risk due to fluctuations in the exchange rate between those two currencies.

On July 21, 2005, the PRC government changed its decade-old policy of pegging the value of the RMB to the U.S. dollar. Under the new policy, the RMB is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies, including the U.S. dollar. This change in policy has resulted in approximately 17% appreciation of the RMB against the U.S. dollar. The PRC government may decide to adopt an even more flexible currency policy in the future, which could result in further and more significant appreciation of the RMB against the U.S. dollar.

A majority of our revenues and expenses relating to hardware sales, the software and service components of our business are denominated in RMB. The value of our shares will be affected by the foreign exchange rate between US dollars and RMB because the value of our business is effectively denominated in RMB, while our shares are traded in US dollars. Furthermore, an increase in the value of the RMB may require us to exchange more US dollars into RMB in order to meet the working capital requirements of our subsidiaries in China. Depreciation of the value of the US dollar will also reduce the value of the cash we hold in US dollars, which we may use for purposes of future acquisitions or other business expansion.

We use U.S. dollars as our reporting and functional currency. The financial records of our Chinese subsidiaries are maintained in RMB, their functional currency. Their assets and liabilities are translated into U.S. dollars based on the rates of exchange existing on the balance sheet date. Their statements of operations are translated using a weighted average rate for the period. Foreign currency translation adjustments are reflected as accumulated other comprehensive income (loss) in stockholders equity. Fluctuation in exchange rate might result in significant foreign currency translation adjustments. We reported foreign currency translation adjustments of $6.5 million, $7.0 million and $2.6 million in other comprehensive income (loss) in 2008, 2007 and 2006, respectively.

The markets in which we sell our services and products are competitive and we may not be able to compete effectively.

We operate in a highly competitive environment, both in the telecommunications software market and in the market for IT security services and solutions. In the telecommunications software market, our competitors include both multinational and local companies such as Amdocs, Digital China, Huawei, Linkage and Neusoft. In the IT security services and solutions market, our competitors include local players such as Topsec and international players such as Cisco.

Our competitors, many of whom have greater financial, technical and human resources than we have, may be able to respond more quickly to new and emerging technologies and changes in customer requirements or devote greater resources to the development, promotion and sale of new products or services. It is possible that competition in the form of new competitors or alliances, joint ventures or consolidation among existing competitors may decrease our market share. Increased competition could result in lower personnel utilization rates, billing rate reductions, fewer customer engagements, reduced gross margins and loss of market share, any one of which could materially and adversely affect our profits and overall financial condition.

Political and economic policies of the Chinese government could affect our industry in general and our competitive position in particular.

Since the establishment of the People s Republic of China in 1949, the Communist Party has been the governing political party in China. The highest bodies of leadership are the Politburo of the Communist Party, the Central Committee and the National People s Congress. The State Council, which is the highest institution of government administration, reports to the National People s Congress and has under its supervision various commissions, agencies and ministries, including the Ministry of Industry and Information Technology, or MIIT, the telecommunications regulatory body of the Chinese government. Since the late 1970s, the Chinese government has been reforming the Chinese economic system. Although we believe that economic reform and the macroeconomic measures adopted by the Chinese government has had and will continue to have a positive effect on economic development in China, there can be no assurance that the economic reform strategy will not from time to time be modified or revised. Such modifications or revisions, if any, could have a material adverse effect on the overall economic growth of China. Such developments could reduce, perhaps significantly, the demand for our products and services. Furthermore, changes in political, economic and social conditions in China, adjustments in policies of the Chinese government or changes in laws and regulations could adversely affect our industry in general and our competitive position in particular.

High technology and emerging market shares have historically experienced extreme volatility and may subject you to losses.

The trading price of our shares may be subject to significant market volatility due to investor perceptions of investments relating to China and Asia, as well as developments in the telecommunications industry. In addition, the high technology sector of the stock market frequently experiences extreme price and volume fluctuations, which have particularly affected the market prices of many software companies and which have often been unrelated to the operating performance of those companies.

We may become subject to securities litigation, which is expensive and could result in a diversion of resources.

In the past, periods of volatility in the market price of a particular company s securities have often been followed by the institution of securities class action litigation against that company. Many companies in our industry have been subject to this type of litigation in the past. Moreover we are currently involved in a securities class action litigation as a result of allegedly improper allocation procedures relating to the sale of our common stock in connection with our initial public offering in March 2000. Although we cannot guarantee the outcome of these proceedings, we believe the final result of these actions will have no material effect on our consolidated financial condition, results of operations or cash flows. However, litigation is often expensive and diverts management s attention and resources, and could materially and adversely affect our business.

A significant number of shares of our common stock are or will be eligible for sale in the open market, which could drive down the market price for our common stock and make it difficult for us to raise capital.

As of July 31, 2009, 45,682,506 shares of our common stock were outstanding, and there were approximately 3,716,978 shares of our common stock issuable upon exercise of outstanding stock options and vesting of outstanding performance stock units and restricted stock units. Sales of a large number of shares by our stockholders could materially decrease the market price of our common stock and make it more difficult for us to raise additional capital through the sale of equity or equity-related securities in the future at a time and price that we deem appropriate.

Our stockholders may experience substantial dilution if we raise additional funds through the sale of equity securities. The issuance of a large number of additional shares of our common stock upon the exercise of outstanding options or in an equity financing transaction could cause a decline in the market price of our common stock due to the sale of a large number of shares of our common stock in the market, or the perception that these sales could occur.

The risk of dilution and the resulting downward pressure on our stock price could also encourage investors to engage in short sales of our common stock. By increasing the number of shares offered for sale, material amounts of short selling could further contribute to progressive price declines in our common stock.

Table of Contents

We are subject to anti-takeover provisions that could prevent a change of control and prevent our stockholders from realizing a premium on their common stock.

Our board of directors has the authority to issue up to 10,000,000 shares of our preferred stock. Without any further vote or action on the part of our stockholders, our board of directors has the authority to determine the price, rights, preferences, privileges and restrictions of the preferred stock. This preferred stock, if it is ever issued, may have preference over and harm the rights of the holders of our common stock. Although the issuance of this preferred stock will provide us with flexibility in connection with possible acquisitions and other corporate purposes, such an issuance may make it more difficult for a third party to acquire a majority of our outstanding voting stock.

We currently have authorized the size of our board of directors to be not less than three or more than ten directors. The terms of the office of our current eight-member board of directors have been divided into three classes: Class I, whose term will expire at the annual meeting of the stockholders to be held in 2012; Class II, whose term will expire at the annual meeting of stockholders to be held in 2010; and Class III, whose term will expire at the annual meeting of stockholders to be held in 2011. This classification of the board of directors may have the effect of delaying or preventing changes in our control or management.

We are subject to the provisions of Section 203 of the Delaware General Corporation Law. In general, the statute prohibits a publicly-held Delaware corporation from engaging in a business combination with an interested stockholder for a period of three years after the date when the person became an interested stockholder unless, subject to certain exceptions, the business combination or the transaction in which the person became an interested stockholder is approved in a prescribed manner. Generally, a business combination includes a merger, asset or stock sale, or other transaction resulting in a financial benefit to the stockholder; and an interested stockholder includes any person that owns 15% or more of our outstanding voting stock or that is our affiliate or associate.

Our change of control severance agreements with executive officers may discourage a change of control.

We have entered into change of control severance agreements with most of our executive officers. These agreements provide, among other things, that the executive officers would be entitled to various benefits upon the occurrence of a covered termination (as defined therein) which occurs within one year after a change of control (as defined therein), including payment of one year of base salary and bonus, immediate vesting of 50% of any outstanding unvested stock options held by the executive officer and the provision of medical benefits and housing allowance. If a change of control occurs, and regardless of whether a covered termination takes place, the executive officers may be entitled to accelerated vesting of 50% of any outstanding unvested stock options held by the executive officer. The potential obligations to pay executive officers such severance amounts may discourage a potential acquirer from effecting a change of control.

Failure to comply with the United States Foreign Corrupt Practices Act could subject us to penalties and other adverse consequences.

Since we are a Delaware corporation and a public company in the United States, we are subject to the United States Foreign Corrupt Practices Act, which generally prohibits U.S. companies from engaging in bribery or other prohibited payments to foreign officials for the purpose of obtaining or retaining business. Non-U.S. companies, including some that may compete with our company, are not subject to these prohibitions. Corruption, extortion, bribery, pay-offs, theft and other fraudulent practices may occur in China. We can make no assurance, however, that our employees or other agents will not engage in such conduct for which we might be held responsible.

If our employees or other agents are found to have engaged in such practices, we could suffer severe penalties and other consequences, including adverse publicity and damage to our reputation that may have a material adverse effect on our business, financial condition and results of operations.

We are subject to potential liabilities and anticipate recurring costs in complying with the Sarbanes-Oxley Act.

In July 2002, the Sarbanes-Oxley Act of 2002, or the Act, was signed into law. Among other things, the Act imposes corporate governance, reporting, and disclosure requirements; introduces stricter independence and financial expertise standards for audit committees; and sets stiff penalties for securities fraud. The Act and the related rules and regulations have increased the scope, complexity and costs of our corporate governance, reporting, and disclosure practices, and may increase the risk of personal liability for our directors, chief executive officer, and chief financial officer. Any such liabilities may adversely affect our reputation, our business, or our ability to meet listing criteria.

Section 404 of the Act requires our management and our independent registered public accounting firm to assess our internal controls over financial reporting on an annual basis. During the course of this evaluation, documentation and attestation, we may identify deficiencies that we may not be able to remedy in time to meet the deadline imposed by the Act for compliance with the requirements of Section 404. If we fail to maintain the adequacy of our internal controls, we may not be able to conclude that we have effective internal controls, on an ongoing basis, over financial reporting in accordance with the Act. Moreover, effective internal controls over financial reporting, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to help prevent or detect fraud. Any failure to maintain effective internal controls over financial reporting could result in the loss of investor confidence in the reliability of our financial statements, which in turn could harm our business and negatively impact the trading price of our common stock.

Table of Contents

We are exposed to certain tax risks with respect to tax benefits enjoyed by certain of our subsidiaries in China under the new Enterprise Income Tax Law of the PRC, or the EIT Law.

Our subsidiaries and affiliated entities in China are subject to tax in China. Historically, as foreign-invested enterprises, or FIEs, most of those subsidiaries enjoyed various tax holidays and other preferential tax treatments, which reduced their effective income tax rates to 15% or lower. The EIT Law, which took effect on January 1, 2008, has applied a uniform 25% enterprise income tax rate to all resident enterprises in China, including FIEs. Moreover, the EIT Law applies to enterprises established outside of China with de facto management bodies located in China. Under the implementation regulations to the EIT Law issued by the PRC State Council, de facto management body is defined as a body that has material and overall management and control over the manufacturing and business operations, personnel and human resources, finances and treasury, and acquisition and disposition of properties and other assets of an enterprise. While we do not believe we are a resident enterprise, because ambiguities exist with the interpretation and application of the EIT Law and the implementation regulations, we may be considered a PRC resident enterprise and therefore may be subject to the China enterprise income tax at the rate of 25% on certain of our income. Certain of our subsidiaries in China will continue to enjoy preferential tax rates as they have been qualified as High and New Technology Enterprises, or HNTEs, under the new EIT Law. The official HNTE certificates have been issued to those subsidiaries in December 2008, prior to the filing of their China enterprise income tax returns.

Dividends payable by us to our non-PRC stockholders, and gains on the sales of our common stock, may be subject to withholding taxes under PRC tax laws, which may materially reduce the value of your investment.

The EIT Law and its implementing regulations, effective January 1, 2008, provide that a 10% withholding tax will normally be applicable on dividends payable to non-PRC stockholders which are derived from sources within the PRC, unless otherwise exempted or reduced by tax treaties or similar arrangements. Any gains realized on the transfer of shares by such stockholders may also be subject to a 10% withholding tax if such gains are regarded as income derived from sources within the PRC. The dividends we pay with respect to our common stock, or the gain our non-PRC stockholders may realize from the transfer of our common stock, may be treated as PRC-sourced income and may therefore be subject to a 10% PRC withholding tax. The EIT Law and its implementing regulations are, however, relatively new and ambiguities exist with respect to the interpretation and identification of PRC-sourced income. If we are required under the EIT Law and its implementing regulations to withhold PRC income tax on dividends payable to our non-PRC stockholders, or if non-PRC stockholders are required to pay PRC income tax on gains on the transfer of their shares of common stock, the value of your investment may be materially reduced.

ITEM 6. EXHIBITS
(a) Exhibits

Please see Exhibit Index.

Table of Contents

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, AsiaInfo Holdings, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

	AsiaInfo Holdings, Inc.	
Date: August 7, 2009	By:	/s/ Wei Li
	Name:	Wei Li
	Title:	Chief Financial Officer

39

Table of Contents

EXHIBIT INDEX

The following exhibits are filed as a part of this Report.

			Incorporated by Reference			
Exhibit No	**Exhibit Title**	**Filed Herewith**	**Form**	**Exhibit No.**	**File No.**	**Filing Date**
10.1*	Master Executive Employment Agreement between AsiaInfo Holdings, Inc. and Jie Li, dated June 10, 2009	X				
10.2*	Change-of-Control Severance Agreement between AsiaInfo Holdings, Inc. and Jie Li, dated June 10, 2009	X				
10.3*	Employment Contract between AsiaInfo Technologies (China), Inc. and Jie Li, dated June 10, 2009 (English Translation)	X				
10.4*	Confidentiality and Non-Competition Agreement between AsiaInfo Technologies (China), Inc. and Jie Li, dated June 10, 2009 (English Translation)	X				
31.1	Certification of Principal Executive Officer required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated August 7, 2009	X				
31.2	Certification of Principal Financial Officer required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated August 7, 2009	X				
32.1	Certification of Chief Executive Officer pursuant to 18 USC. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated August 7, 2009	X				
32.2	Certification of Chief Financial Officer pursuant to 18 USC. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated August 7, 2009	X				

* Management contract, or compensatory plan or arrangement.