



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

**FORM 20-F**

(Mark One)

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

**OR**

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

**For the fiscal year ended December 31, 2013**

**OR**

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

**OR**

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

**Commission file number: 001-34271**

**CHANGYOU.COM LIMITED**

**(Exact name of Registrant as specified in its charter)**

**N/A**

**(Translation of Registrant's name into English)**

**Cayman Islands**

**(Jurisdiction of incorporation or organization)**

**East Tower, Jing Yan Building  
No. 29 Shijingshan Road, Shijingshan District  
Beijing 100043  
People's Republic of China  
(Address of principal executive offices)**

**Alex Ho  
Chief Financial Officer**



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

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

<u>(Title of each class)</u>	<u>(Name of each exchange on which registered)</u>
American Depositary Shares, each representing two Class A ordinary shares, par value US\$0.01 per share	The NASDAQ Global Select Market

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

None

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

None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 23,184,186 Class A ordinary shares, par value \$0.01 per share, and 82,490,000 Class B ordinary shares, par value \$0.01 per share, as of December 31, 2013.

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

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐

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

U.S. GAAP ☒ International Financial Reporting Standards as issued by the International Accounting Standards Board ☐ Other ☐

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

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



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## Introduction

In this annual report, except where the context otherwise requires and for purposes of this annual report only:

- “17173 Business” refers to the assets and business operations associated with our online game information portal operated through the 17173.com Website;
- “7Road” refers to 7Road.com Limited, a Cayman Islands company, and unless the context requires otherwise, includes its subsidiaries and variable interest entity;
- “ADSs” refers to our American depositary shares, each of which represents two Class A ordinary shares, par value \$0.01 per share;
- “Changyou” refers to Changyou.com Limited, a Cayman Islands company, and unless the context requires otherwise, includes its subsidiaries and variable interest entities;
- “China” or “PRC” refers to the People’s Republic of China, and for the purpose of this annual report, excludes Hong Kong, Macau and Taiwan;
- “Doyo” refers to Beijing Doyo Internet Technology Co., Ltd., which we acquired in November 2013 through our variable interest entity Beijing Guanyou Gamespace Digital Technology Co., Ltd., or Guanyou Gamespace, as a wholly-owned subsidiary of Guanyou Gamespace;
- “RaidCall” refers to free social communication software that facilitates real-time online group activities via voice, text and video, allowing users to create and organize groups of varying size to participate in a wide range of online group activities, such as online games, music, and karaoke and other live performance dynamics;
- “RaidCall Business” refers to the assets associated with RaidCall, which were acquired by Changyou;
- “MMOGs” refers to massively multiplayer online games, which are interactive online games that may be played simultaneously by hundreds of thousands of game players. MMORPGs and MMOFPSs are subsets of the MMOG category;
- “MMORPGs” refers to massively multiplayer online role-playing games;
- “MMOFPSs” refers to massively multiplayer first-person shooter games;
- “PRC GAAP” refers to generally accepted accounting principles of the PRC;
- “Sohu.com Inc.” refers to our ultimate parent and controlling shareholder, whose shares of common stock are listed on the NASDAQ Global Select Market under the symbol “SOHU;”
- “Sohu” refers to Sohu.com Inc. and its subsidiaries and consolidated variable interest entities and, unless the context requires otherwise, excludes Changyou.com Limited and its subsidiaries and variable interest entities;
- “Sohu Group” refers to Sohu.com Inc. and its subsidiaries and consolidated variable interest entities and, unless the context requires otherwise, includes Changyou.com Limited and its subsidiaries and variable interest entities;
- “TLBB,” “BO,” “BH2,” “DMD,” “DHS,” “JY,” “SZHG,” “DPCQ,” and “YZZX,” refer to “Tian Long Ba Bu,” “Blade Online,” “Blade Hero 2,” “Duke of Mount Deer,” “Da Hua Shui Hu,” “Jian Ying,” “Shen Zhi Huang Guan,” “Dou Po Cang Qiong,” and “Yong Zhe Zhi Xin,” respectively;
- “U.S. GAAP” refers to generally accepted accounting principles in the United States; and
- “we,” “us,” “our company” and “our” refer to Changyou.com Limited, and unless the context requires otherwise, include its subsidiaries and variable interest entities.

All references to “RMB” or “Renminbi” refer to the legal currency of China; all references to “US\$,” “dollars,” “U.S. dollars” and “\$” refer to the legal currency of the United States.

This annual report on Form 20-F includes our audited consolidated statements of comprehensive income for the years ended December 31, 2011, 2012 and 2013 and audited consolidated balance sheets as of December 31, 2012 and 2013.

We completed an initial public offering of our ADSs on April 7, 2009. Our ADSs are traded on the NASDAQ Global Select Market under the symbol “CYOU.”



## FORWARD-LOOKING INFORMATION

This annual report on Form 20-F contains “forward looking statements.” These statements are made under the “safe harbor” provisions of the U.S. Private Securities Litigation Reform Act of 1995. You can identify these forward-looking statements by terms such as “may,” “will,” “expects,” “anticipates,” “future,” “intend,” “plan,” “believe,” “estimate,” “is/are likely to” and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements. The forward-looking statements made in this annual report relate only to events as of the date on which the statements are made. We undertake no obligation, beyond any than as required by law, to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made, even though our situation will change in the future.

These forward-looking statements include, but are not limited to, the following:

- our ability to maintain and strengthen our position as a leading provider of products and services to online gamers in China;
- our expected development, launch and market acceptance of additional MMOGs and Web and mobile games;
- our ability to maintain and strengthen our 17173.com Website as a leading game information portal in China;
- our various initiatives to implement our business strategies to expand our business through organic growth and strategic acquisitions;
- our future business development, results of operations and financial condition;
- the expected growth of and change in the online game industry in China; and
- the PRC government policies relating to the Internet and Internet content providers, including online game developers and operators.

We operate in an emerging and evolving environment. New risk factors emerge from time to time and it is impossible for our management to predict all risk factors, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statement.

We would like to caution you not to place undue reliance on forward-looking statements and you should read these statements in conjunction with all other parts of this annual report, including the risk factors set forth in Item 3. See “Key Information—Risk Factors.”

## PART I

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

Not Applicable.

### ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not Applicable.

### ITEM 3. KEY INFORMATION

#### *Selected Consolidated Financial Data*

The following table presents the selected consolidated financial information for our company. The selected consolidated statements of comprehensive income data for the three years ended December 31, 2011, 2012 and 2013 and the consolidated balance sheets data as of December 31, 2012 and 2013 have been derived from our audited consolidated financial statements included in this annual report beginning on page F-1. The selected consolidated statements of comprehensive income data for the years ended December 31, 2009 and 2010 and our consolidated balance sheets data as of December 31, 2009, 2010 and 2011 have been derived from audited consolidated financial statements that are not included in this report. The selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements and related notes and “Item 5. Operating and Financial Review and Prospects” below. Our consolidated financial statements are prepared and presented in accordance with U.S. GAAP. Our historical results do not necessarily indicate results expected for any future periods.

As the 17173 Business and Changyou were under common control by Sohu both before and after our acquisition of the 17173 Business on December 15, 2011, the consolidated financial data presented below have been prepared as if we had owned the assets of and operated the 17173 Business throughout the periods presented, and the consolidated financial data for the years ended December 31, 2009, and 2010 have been restated accordingly. The consolidated financial data set forth below as of and for each of the years presented may not necessarily reflect the results of operations, financial position and cash flows we would have experienced with respect to the 17173 Business if we had owned and operated it throughout those years.

	For the Year Ended December 31,				
	2009	2010	2011	2012	2013
	(\$ in thousands, except for share, per share and per ADS data)				
<b>Consolidated Statement of Comprehensive Income Data:</b>					
Revenues:					
Online game	267,585	327,153	435,512	570,346	669,168
Online advertising	20,617	25,988	36,349	42,525	49,998
IVAS	—	965	1,862	4,307	5,402
Others	—	—	10,853	6,251	13,307
Total revenues	288,202	354,106	484,576	623,429	737,875
Cost of revenues: <sup>(1)</sup>					
Online game	17,518	29,852	49,837	76,432	93,306
Online advertising	2,431	3,154	3,892	6,535	13,827
IVAS	—	—	—	1,509	1,786
Others	—	—	13,783	20,046	17,518
Total cost of revenues	19,949	33,006	67,512	104,522	126,437
Gross profit	268,253	321,100	417,064	518,907	611,438
Operating expenses:					
Product development <sup>(1)</sup>	28,864	39,893	52,238	73,755	119,909
Sales and marketing <sup>(1)</sup>	36,348	39,211	49,893	60,639	128,830
General and administrative <sup>(1)</sup>	20,052	19,558	29,684	33,514	57,191
Goodwill impairment and impairment of acquired intangibles via acquisition of businesses	—	—	5,420	2,906	—
Total operating expenses	85,264	98,662	137,235	170,814	305,930
Operating profit	182,989	222,438	279,829	348,093	305,508
Interest income	3,391	4,194	11,933	15,882	28,455
Foreign currency exchange loss	(12)	(527)	(618)	(558)	(5,936)
Interest expense	(104)	(39)	(7)	(2,243)	(8,835)
Other income (expense)	159	(1,393)	457	(173)	3,613
Income before income tax expense	186,423	224,673	291,594	361,001	322,805
Income tax expense	24,205	29,990	43,580	67,405	36,383
Net income	162,218	194,683	248,014	293,596	286,422
Less: Net income attributable to the mezzanine classified non-controlling interest	—	—	2,558	11,196	17,780
Net income attributable to Changyou.com Limited	162,218	194,683	245,456	282,400	268,642
Net income	162,218	194,683	248,014	293,596	286,422
Other comprehensive income: Foreign currency translation adjustment	151	10,291	21,867	3,385	33,600
Comprehensive income	162,369	204,974	269,881	296,981	320,022
Comprehensive income attributable to the mezzanine classified non-controlling interest	—	—	2,558	11,196	17,780
Comprehensive income attributable to Changyou.com Limited	162,369	204,974	267,323	285,785	302,242
Cash dividend per share	0.96	—	—	1.90	—
Basic net income per share	1.61	1.88	2.34	2.67	2.53
Diluted net income per share	1.57	1.83	2.30	2.64	2.52
Basic net income per ADS	3.22	3.75	4.68	5.35	5.06
Diluted net income per ADS	3.15	3.66	4.61	5.29	5.04
Weighted average number of ordinary shares outstanding, basic	100,728	103,792	104,854	105,656	106,252
Weighted average number of ordinary shares outstanding, diluted	103,051	106,239	106,600	106,792	106,676
Weighted average number of ADS outstanding, basic	50,364	51,896	52,427	52,828	53,126
Weighted average number of ADS outstanding, diluted	51,526	53,120	53,300	53,396	53,338



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CHANGYOU.COM LIMITED

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(1) Share-based compensation expenses are included in the following financial statements line items:

	For the Year Ended December 31,				
	2009	2010	2011	2012	2013
	(\$ in thousands)				
Cost of revenues	356	430	230	306	101
Product development	7,419	4,465	2,399	1,854	475
Sales and marketing	304	569	960	326	74
General and administrative	5,418	4,098	2,528	1,183	624

### Selected Consolidated Balance Sheet Data

	As of December 31,				
	2009	2010	2011	2012	2013
	(\$ in thousands)				
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	226,950	351,027	330,411	366,639	548,484
Restricted time deposits	—	—	—	246,599	424,674
Accounts receivable, net	8,040	6,743	11,326	23,364	35,996
Short-term investments	—	—	17,560	51,720	2,827
Fixed assets, net	50,014	54,641	68,394	64,828	246,674
<b>Total assets</b>	<b>313,939</b>	<b>528,373</b>	<b>753,073</b>	<b>1,114,513</b>	<b>1,585,212</b>
Receipts in advance and deferred revenue	30,452	36,237	51,900	43,659	43,842
Short-term bank loans	—	—	—	113,000	410,331
Long-term bank loans	—	—	—	126,353	—
<b>Total liabilities</b>	<b>77,526</b>	<b>100,867</b>	<b>180,958</b>	<b>444,818</b>	<b>671,696</b>
Mezzanine equity	—	—	57,254	61,810	—
Total shareholders' equity	236,413	427,506	514,861	607,885	913,516
<b>Total liabilities, mezzanine equity and shareholders' equity</b>	<b>313,939</b>	<b>528,373</b>	<b>753,073</b>	<b>1,114,513</b>	<b>1,585,212</b>

### Risk Factors

#### *Risks Relating to Our Business and Our Industry*

*Our limited operating history makes evaluating our business and prospects difficult.*

We were incorporated on August 6, 2007 in the Cayman Islands as an indirect wholly-owned subsidiary of Sohu.com Inc. Sohu transferred all of its MMOG business to us in December 2007. We acquired the entities operating our cinema advertising business in January 2011; we acquired a majority interest in 7Road in May 2011 and acquired all of the remaining equity interests in 7Road in June 2013; we acquired the 17173 Business, which operates our online advertising business, from Sohu in December 2011; and we acquired several other entities offering Internet software products in 2013. Our limited operating history in each of these areas may not provide a meaningful basis for you to evaluate our business and prospects. Our business strategy has not been proven over a long period of time and we cannot be certain that we will be able to successfully expand our online games business, our online advertising business, the Internet value-added services, or IVAS, business and our cinema advertising business.

You should also consider additional risks and uncertainties that may be experienced by early stage companies operating in a rapidly developing and evolving industry. Some of these risks and uncertainties relate to our ability to:

- develop, license or operate new MMOGs and Web and mobile games that are appealing to game players and meet our expected timetable for launches of new games;
- raise our brand recognition and game player loyalty;
- maintain and strengthen the 17173 Business and the leading position of the 17173.com Website among game information portals in China;
- successfully adapt to evolving business models, industry trends and market environments by developing and investing in new business strategies, products, services and technologies, including new games other than MMOGs and Web games, such as social games and mobile games, and new software for mobile devices; and
- maintain or expand our marketing efforts to attract more game players to our games and to the game information portal of the 17173 Business and to the various Internet software products and software for mobile devices developed or acquired by us in an increasingly competitive business environment.





If we do not adapt our business to address these risks and uncertainties, our ability to continue our success to date or to expand our business in the future may be impeded.

*Our business may not succeed in a highly competitive market.*

Competition in the online game market in China is becoming increasingly intense. There are a number of publicly-traded companies focusing on the MMOG and/or Web games markets in China with shares listed on NASDAQ, the New York Stock Exchange, the Hong Kong Stock Exchange and the Shenzhen Stock Exchange, including Tencent Holdings Limited, NetEase.com, Inc., Shanda Games Limited, Perfect World Co., Ltd., Giant Interactive Group Inc., NetDragon Websoft Inc., Kingsoft Corporation Limited, Taomee Holdings Limited, Shenzhen ZQGame Co., Forgame Holdings Limited, and YY Inc.

In addition, there are many venture-backed private companies focusing on online game development, further intensifying the competition. Recently, many of our competitors have been aggressively hiring talent for game development, increasing spending on marketing for games, bidding for licenses of games, penetrating into the Web and mobile game markets, and releasing new software for mobile devices to attract a growing number of gamers that access Internet products and services through mobile devices. Increased competition in our current and intended markets may make it difficult for us to retain our existing employees and attract new employees, and to sustain our growth rate. Furthermore, we also face intense competition for cost-effective marketing resources for our games, such as game-related Websites, which could drive up our marketing costs and decrease the effectiveness of our marketing campaigns.

The 17173 Business, which derives revenue primarily from providing advertising services to advertisers on the 17173.com Website, faces intense competition for advertising business targeting online game players, which can be expected to increase significantly in the future. We compete with other game information portals, such as duowan.com, operated by YY Inc., and game.qq.com, operated by Tencent Holdings Ltd., and other Internet portals which have, or may over time be able to build, competitive advantages over us in terms of:

- greater brand recognition among game players and advertising clients;
- larger user and customer bases;
- more extensive and well developed marketing and sales networks; and
- substantially greater financial and technical resources.

If we are unable to sustain and enhance our brand recognition, provide quality products and services and meet other difficult technological and business challenges, then our users and advertising clients may become dissatisfied and move to a competitor's portal for products and services, our user base may decrease and our ability to generate advertising revenues on our 17173.com Website may decline as a result.

In order to compete effectively in the PRC, as well as in the worldwide market, we must continue to spend significant resources in research and development, including through acquisitions, to enhance our technology and our existing games, advertising and other services, introduce new game products and services, including games other than MMOGs and Web games, such as mobile games, new software for mobile devices, in order for us to adapt to industry trends and shifting demands of game players and advertising clients and to remain competitive. If our products and services are not responsive to the needs of our game players and advertisers, are not appropriately timed with market opportunities, or are not effectively brought to market, or if our competitors are more successful than we are in developing compelling products or in attracting and retaining game players and advertisers, we may not be able to recoup such expenditures.

*There are uncertainties regarding the future growth of the online game industry in China.*

The online game industry, from which we derive substantially all of our revenues, is a relatively new and evolving industry. The growth of the online game industry and the level of demand and market acceptance of our games are subject to a high degree of uncertainty. Our future operating results will depend on numerous factors affecting the online game industry, many of which are beyond our control, including:

- whether recent declines in the use of personal computers in general, and for purposes of accessing online games in particular, continue or accelerate in China and other markets in which we offer our games;
- the growth of mobile device (such as smart phones and tablets), Internet and broadband users and penetration in China and other markets in which we offer our games, and the rate of any such growth;





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- whether the online game industry, particularly in China and the rest of the Asia-Pacific region, continues to grow and the rate of any such growth;
- general economic conditions in China, particularly economic conditions adversely affecting discretionary consumer spending, such as the slowdown in China's economic growth that occurred between the first quarter of 2010 and the third quarter of 2012;
- the availability and popularity of other forms of entertainment, particularly games of console systems, which are already popular in developed countries and may gain popularity in China; and
- changes in consumer demographics and public tastes and preferences.

There is no assurance that online games, and in particular MMOGs and Web games, will continue to be popular in China or elsewhere. A decline in the popularity of online games in general, or the MMOGs and Web games that we operate, would adversely affect our business and prospects.

*We currently depend on TLBB for a majority of our revenues and on Wartune and DDTank for a significant portion of our revenues. Any decrease in the popularity of these games or interruption in their operation would adversely affect our results of operations.*

We currently rely on our MMOG TLBB for a majority of our revenues and on our Web games Wartune and DDTank for a significant portion of our revenues. We launched TLBB, Wartune and DDTank in May 2007, December 2011 and March 2009, respectively. We cannot guarantee how long TLBB, Wartune and DDTank, will continue to sustain their current level of popularity. To prolong TLBB's, Wartune's, and DDTank's lifespans, we need to continually improve and update them on a timely basis with new features that appeal to existing game players and attract new game players, and to market these new features. Despite our efforts to improve TLBB, Wartune and DDTank, our game players may nevertheless lose interest in these games over time. See "We may not be successful in operating and improving our games to satisfy the changing demands of game players." If we fail to improve and update these games on a timely basis, or if our competitors introduce more popular games catering to our game player base, which, in the case of TLBB, could include games adapted from other novels written by Louis Cha, these games may lose their popularity, which could cause our revenues to decrease.

Furthermore, there could be interruptions in the operation of TLBB, Wartune or DDTank due to unexpected server interruptions, network failures or other factors that could harm our reputation and prevent or deter game players from making purchases of virtual items, which could result in decreases in our revenues. We do not maintain insurance policies covering losses relating to our technology infrastructure and we do not have business interruption insurance.

*Our revenues are not likely to sustain their recent growth rate; we expect to sustain losses in the near term and we cannot assure you that we can avoid future losses.*

Our revenues have grown significantly in a relatively short period of time. Primarily due to the commercial success of TLBB, our revenues grew from \$484.6 million for the year ended December 31, 2011 to \$623.4 million for the year ended December 31, 2012, and to \$737.9 million for the year ended December 31, 2013. Our net income attributable to Changyou.com Limited grew from \$245.5 million for the year ended December 31, 2011 to \$282.4 million for the year ended December 31, 2012 but decreased to \$268.6 million for the year ended December 31, 2013. We are not likely to sustain similar rates of growth in revenues in future periods. We expect to sustain net losses in the near future due to increased spending for marketing for software on mobile devices. We cannot assure you that we will avoid further net losses or that there will not be any declines or further declines in our revenues for any future periods, due to a number of factors, including, among others, the greater difficulty of growing at sustained rates from a larger revenue base, the uncertain level of popularity of our future games, the need to expend greater amounts in order to develop or acquire new games, technologies, assets, and businesses, and uncertainty as to our ability to integrate such newly acquired games, technologies, assets and businesses. In particular, we expect to experience significant increases in our costs and expenses as we expand our business into mobile games and software for mobile devices in order to adapt to industry trends and an evolving market environment and expand domestically and internationally. Accordingly, you should not rely on the results of any prior period as an indication of our future financial and operating performance.

*Our business could suffer if we do not successfully manage our current and future growth.*

We have experienced a period of rapid growth and expansion that has placed, and will continue to place, strain on our management personnel, systems and resources. To accommodate growth, we anticipate that we will need to implement a variety of new and upgraded operational and financial systems, including online payment systems, procedures and controls, improvement of our accounting and other internal management systems and security systems related to the foregoing, all of which require substantial management efforts and financial resources. We will also need to continue to expand, train, manage and motivate our workforce, and manage our relationships with our distributors and joint operators, third-party service providers and game player base. All of these endeavors will require substantial management effort and skills and the incurrence of additional expenditures. We may not be able to efficiently or effectively implement our growth strategies and manage the growth of our operations, and any failure to do so may limit our future growth and hamper our business strategy.



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*Recent and potential future acquisitions and/or strategic alliances may have an adverse effect on our ability to manage our business and may also result in impairment charges.*

We have made acquisitions of, and may potentially acquire in the future, technologies, businesses or assets that are complementary to our business and/or enter into strategic alliances in order to leverage our position in the Chinese online game market and expand our business domestically and internationally. Such acquisitions or strategic alliances may expose us to potential risks, including risks associated with the integration of new technologies, businesses and personnel, unforeseen or hidden liabilities, the diversion of management attention and resources from our existing business, and the inability to generate sufficient revenues to offset the costs and expenses of acquisitions or strategic alliances. Any difficulties encountered in the acquisition and strategic alliance process may have an adverse effect on our ability to manage our business. In addition, acquired businesses may not perform to our expectations for various reasons, including the loss of key personnel or key clients, and our strategic focus may change. As a result, we may not realize the benefits we anticipated. If we fail to integrate acquired technologies, businesses and assets or realize the expected benefits, we may not receive a return on our investment and our transaction costs for such acquisitions. The benefits of an acquisition or investment may also take considerable time to develop, and we cannot be certain that any particular acquisition or investment will produce the intended benefits, which could adversely affect our business and operating results. Acquisitions could result in contingent liabilities or amortization expenses related to intangible assets or write-offs of goodwill and/or intangible assets, which could adversely affect our results of operations.

*We are party to an agreement with Sohu that limits our ability to enter certain businesses.*

We are a party to an Amended and Restated Non-Competition Agreement with Sohu which prohibits us, during the non-competition period, from engaging in certain businesses that Sohu conducted or contemplated conducting as of April 1, 2009, not including the MMORPG business and the 17173 Business. See “Major Shareholders and Related Party Transactions” in Item 7 of this annual report. As a result, during such non-competition period, we will not be able to diversify our business into online portal, search, mobile value-added services and other businesses, other than the MMORPG business and the 17173 Business, that Sohu was conducting, or contemplated conducting, as of that date, even if such businesses present growth opportunities for us. In addition, the Amended and Restated Non-Competition Agreement does not prohibit Sohu from engaging in the development and operation of online games other than MMORPGs, even during the non-competition period. Any online games (other than MMORPGs) that we develop and operate that are not prohibited under the Amended and Restated Non-Competition Agreement may face competition from other online games, including those developed and/or operated by Sohu.

*Our marketing and promotion have benefited from our association with Sohu. Any negative development in Sohu’s market position or brand recognition may have an adverse effect on our marketing efforts and the popularity of our games.*

We are a majority-owned subsidiary of Sohu and expect to continue to be part of the Sohu Group, as Sohu is expected to remain our controlling shareholder. We have benefited, and expect to continue to benefit, from Sohu in marketing our games and the 17173 Business. For example, we have benefited from Sohu’s large user base by marketing and advertising across Sohu’s domains and using the Sohu Group’s single-user ID system, which provides Sohu’s registered users easy access to our games. We and Sohu have entered into a services agreement and an online links and advertising agreement, pursuant to which Sohu provides links and advertising space on Sohu’s Websites and related technical support to us in connection with our operation and promotion of the 17173 Business. We also benefit from Sohu’s strong brand recognition in China, which we believe has provided us credibility and a broad marketing reach.

If Sohu loses its market position, the effectiveness of our marketing efforts through our association with Sohu could be adversely affected. In addition, any negative publicity associated with Sohu.com or its affiliated Websites will likely have an adverse impact on the effectiveness of our marketing on those sites as well as our reputation and our brand.

*We are dependent upon our management, our key development and technical personnel; our Chief Financial Officer has resigned and our business may be severely disrupted if we are unable to find a replacement or if we lose the services of other members of our management or key personnel.*

Our future success depends substantially on the continued services of our executive officers and our key development personnel, such as our Chief Executive Officer Tao Wang, our President Dewen Chen, our Chief Operating Officer Xiaojian Hong and our Chief Information Officer Wendy Pan. If one or more of our executive officers or key development personnel were unable or unwilling to continue in their present positions, we might not be able to replace them easily or at all. For example, our Chief Financial Officer Alex Ho resigned effective March 4, 2014 and, although we have designated an interim replacement, we have not yet identified a permanent replacement for Mr. Ho. Our business could be significantly disrupted if we are not successful in identifying and hiring a replacement for Mr. Ho. In addition, if any of our executive officers or key employees joins a competitor or forms a competing company, we may lose know-how, key professionals, staff members and suppliers. These executive officers and key employees could develop and operate games that could compete with and take game players away from our existing and future games. Although each of our executive officers and key personnel has entered into an employment agreement with us with non-competition provisions, these non-competition provisions may not be enforceable in China.



*Game players' spending on our games may be adversely affected by continuing slower growth in the Chinese economy and adverse conditions in the global economy.*

We rely on the spending of our game players for our revenues, which in turn depends on the players' level of disposable income, perceived future earnings capabilities and willingness to spend. The real estate market in the PRC and the level of exports from the PRC have both experienced significant declines recently and, according to the National Bureau of Statistics of China, the growth rate of China's gross domestic product, compared to that of the previous year, slowed from 10.3% in 2010 to 9.2% in 2011 and 7.5% in 2012 and 7.7% in 2013. Such growth may continue to slow in the future, which could in turn result in a reduction in spending by our game players.

In addition, the global economy has experienced significant instability in recent years, with growth in the United States slowing and the European Community facing disruptions as a result of crises in the economies of Greece and Spain, among other countries. It is unclear how long instability will continue, whether it will increase, whether it will lead to a renewed worldwide economic downturn such as the one that began in 2008, and how much adverse impact such instability or any such downturn might have on the economies of China and other jurisdictions where we operate our games. Any such instability or adverse impact in China or in overseas markets could cause our game players to reduce their spending on our games in China or overseas and reduce our revenues.

*We may not be successful in operating and improving our games to satisfy the changing demands of game players.*

We depend on purchases and continual consumption of virtual items by our game players to generate revenues, which in turn depend on the continued attractiveness of our games to the game players and their satisfactory game-playing experience. Various issues could arise that would cause our games to be less attractive to our game players or could limit the continued attractiveness of our games. For example:

- we may fail to provide game updates, expansion packs and other enhancements in a timely manner due to technologies, resources or other factors;
- our game updates, expansion packs and new versions may contain program errors, and their installation may create other unforeseen issues that adversely affect the game-playing experience;
- we may fail to timely respond and/or resolve complaints from our game players;
- we may fail to eliminate computer "bots" which can disrupt our games' smooth operation and reduce the attractiveness of our games; and
- our game updates, expansion packs and other enhancements may change rules or other aspects of our games that our game players do not welcome, resulting in a reduction in the active accounts, peak concurrent users, active paying accounts, average concurrent users, and/or revenues per active paying account of our MMOGs or a reduction in the active accounts, active charging accounts, peak concurrent users, average concurrent users and/or revenues per active charging account of our Web games.

Our failure to address the above-mentioned issues could adversely affect the game-playing experience of our game players, damage the reputation of our games, shorten the lifespans of our games, and result in the loss of game players and a decrease in our revenues.

Furthermore, for the games that we license from third parties, we may not have access to the game source codes during the initial period of the license or at all. Without the source codes, we have to rely on the licensors to provide updates and enhancements during the initial period, giving us less control over the quality and timeliness of updates and enhancements. If our game players are not satisfied with the level of services they receive, they may choose to not play the games, leading to a decrease in our revenues.

*We may fail to launch new games according to our timetable, and our new games may not be commercially successful, or may attract game players away from our existing games.*

We must launch new games that can generate additional revenue and diversify our revenue sources in order to remain competitive. We will not generate any meaningful revenue from a pipeline game until it is commercially launched after open beta testing, and we cannot assure you that we will be able to meet our timetable for new game launches or that our new games will be successful. A number of factors, including technical difficulties, lack of sufficient game development personnel and other resources, failure to obtain or delays in obtaining relevant governmental authorities' approvals and adverse developments in our relationships with the licensors or third-party operators of our new games could result in delayed launching of our new games. In addition, we cannot assure you that our new games will be as well received in the market as TLBB, Wartune and DDTank have been, and you should not view our historical game revenues or the success of TLBB, Wartune and DDTank as indications of the commercial success of any of our new or future games. We may fail to anticipate and adapt to future technical trends, new business models and changed game player preferences and requirements, fail to effectively plan and organize marketing and promotion activities, or fail to differentiate our new games from our existing games. If the new games we introduce are not commercially successful, we may not be able to generate sufficient revenues from new games to sustain or grow our results of operations or to recover our product development costs and sales and marketing expenses, which can be significant.



In addition, our new games may attract game players away from our existing games. For example, with our increasingly diversified game portfolio, we cannot assure you that our TLBB, Wartune and DDTank game players will not be attracted to play other newly launched games instead of TLBB, Wartune and DDTank. If this occurs, it will decrease our existing games' player bases, which could in turn make these games less attractive to other game players, resulting in decreased revenues from our existing games. Game players who switch from playing our existing games to our new games may also spend less money to purchase virtual items in our new games than they would have spent if they had continued playing our existing games, resulting in an adverse effect on our overall revenues.

*Our MMOGs and Web games are currently accessed primarily through personal computers. As devices other than personal computers are increasingly used to access the Internet, we believe that we must acquire or develop software and games for such devices if we are to maintain or increase our revenues, and we may not be successful in doing so.*

Devices other than personal computers, such as mobile phones and tablets, are used increasingly in China and in overseas markets to access the Internet. We believe that, for our business to be successful, we will need to develop versions of our existing games, our pipeline games and any future games that work well with such devices. The games that we develop for such devices may not function as smoothly as our existing games, and may not be attractive to game players in other ways. In addition, manufacturers of such devices may establish restrictive conditions for developers of applications to be used on such devices, and as a result our games may not work well, or at all, on such devices. As new devices are released or updated, we may encounter problems in developing versions of our games for use on such devices and we may need to devote significant resources to the creation, support, and maintenance of games for such devices. During 2013, in order to pursue opportunities arising from the global trend toward mobile Internet, we invested significant amounts in the acquisition, development and operation of software and games for mobile devices, and we expect to continue to make considerable expenditures during 2014 in order to launch selected software, games and platforms for the mobile market. If we are unable to successfully expand the types of devices on which our existing and future games are available, or if the versions of our games that we create for such devices do not function well or are not attractive to game players, or if the software and mobile games for mobile devices that we have launched, or expect to launch in the future, are not successful, we may not be able to recoup our investments in the mobile market.

*Our business will suffer if we are unable to develop successful games for mobile platforms or successfully monetize mobile games we develop or acquire.*

Developing games for mobile devices is an important component of our strategy. We have devoted and we expect to continue to devote substantial resources to the development of our mobile games, and we cannot guarantee that we will be able to develop games that appeal to players. In addition, we may encounter difficulty in integrating features on games developed for mobile devices that a sufficient number of players will pay for or otherwise sufficiently monetizing mobile games. Generally, our mobile games monetize at a lower rate than our Web games and we may not be successful in our efforts to increase our monetization from mobile games. If we are unable to implement successful monetization strategies for our mobile games, our ability to grow revenue and our financial performance will be negatively affected.

Our ability to successfully develop games for mobile devices will depend on our ability to:

- expand the portfolio of mobile games that we develop in-house and license from third-party developers;
- effectively develop new mobile games for multiple mobile operating systems and mobile devices;
- effectively cross-market mobile games to players of our current MMOG, Web games and mobile games;
- anticipate and effectively respond to the growing number of players switching from Web games to mobile games, the changing mobile landscape and the interests of players;
- attract, retain and motivate talented game designers, product managers and engineers with experience in developing games for mobile devices;
- minimize launch delays and cost overruns on the development of new games;



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- effectively monetize mobile games without degrading the social game experience for our players;
- develop games that provide for a compelling and optimal user experience through existing and developing third party technologies, including third party software and middleware utilized by our players; and
- acquire and successfully integrate high quality mobile game assets, personnel or companies.

These and other uncertainties make it difficult to know whether we will succeed in developing successful mobile games. If we do not succeed in doing so, our business will suffer.

*We rely on third-party operators to jointly operate most of our Web games with us.*

We largely rely on third-party joint operators to attract users to play our Web games and for most of the marketing of such games. Operations through third-party joint operators account for a substantial majority of our revenues from Web games. If third-party joint operators of our games experience network disruptions, cease to offer our games over their platforms, fail to effectively promote our games on their platforms or attract game players, or terminate our joint operation agreements in advance of their expiration dates during any particular period, our revenues for that period will be adversely affected and our reputation and/or the reputation of our subsidiaries that are engaged in game development could be harmed.

*We generate substantially all of our game revenues under the item-based revenue model, which has a short history of commercial application and presents risks related to consumer preferences and regulatory restrictions.*

Substantially all of our games, including MMOGs, Web games and mobile games, are operated under the item-based revenue model. Under this revenue model, our game players are able to play the games for free if they so choose, but are charged for the purchase of virtual items in the games. We currently expect that substantially all of our game revenues, including revenues from games currently in our pipeline, will continue to be generated under the item-based revenue model. The item-based revenue model requires us to design games that not only attract game players to spend more time playing, but also encourage them to purchase virtual items. The sale of virtual items requires us to track closely consumer tastes and preferences, especially as to in-game consumption patterns. If we fail to design and price virtual items so as to incentivize game players to purchase them, we may not be able to effectively translate our game player base and their playing time into revenues. The item-based revenue model does not have a long history of proven commercial application. In addition, the item-based revenue model may cause additional concerns with PRC regulators who have been implementing regulations designed to reduce the amount of time that Chinese youths spend on online games and intended to limit the total amount of virtual currency issued by online game operators and the amount purchased by individual game players. A revenue model that does not charge for time played may be viewed by the PRC regulators as inconsistent with these goals. The item-based revenue model may not continue to be commercially successful and in the future we may need to change our revenue model to a time-based or other revenue model. Any change in revenue model could result in disruption of our game operations, a decrease in the number of our game players and a decline in our revenues.

*We rely on recorded data for game revenue recognition and tracking of game players' consumption patterns of virtual items. If our data systems fail to operate effectively, such failure will not only affect the completeness and accuracy of our revenue recognition, but also our ability to design and improve virtual items that appeal to game players.*

Our game operations revenues are generated through the sale of our prepaid game cards or online direct sale of game points, and our recognition of those revenues depends on such factors as whether the virtual items purchased by game players are considered consumable or perpetual and, in the case of our Web game joint operation arrangements with third-party joint operators, whether the games are hosted on our servers or the third parties' servers. We rely on our data systems to record and monitor the purchase and consumption of virtual items by our game players and the types of virtual items purchased. If our data systems fail to accurately record the purchase and consumption information of the virtual items, we may not be able to accurately recognize our revenues. In addition, various factors affect the estimated lives of perpetual virtual items, such as the average period that game players typically play our games and other game player behavior patterns, the acceptance and popularity of expansion packs, promotional events launched and market conditions, and we rely on our billing systems to capture such historical game player behavior patterns and other information. If such information is not accurately recorded, or if we do not have sufficient information due to the short operating history of any of our games, we will not be able to accurately estimate the lives of, or the estimated average period the game players play our games with respect to, the perpetual virtual items, which will also affect our ability to accurately recognize our revenues from such perpetual virtual items. If our data systems were damaged by system failure, network interruption, or virus infection, or attacked by a hacker, the integrity of data would be compromised, which could adversely affect our revenue recognition and the completeness and accuracy of our recognized revenues.

In addition, we rely on our data systems to record game player purchase and consumption patterns, based on which we improve our existing virtual items and design new virtual items. For example, we intend to increase development efforts on the number and variety of virtual items that our game players like to purchase, and we may also adjust prices accordingly. If our data systems fail to record data accurately, our ability to improve existing virtual items or design new virtual items that are appealing to our game players may be adversely affected, which could in turn adversely affect our revenues.





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*The successful operation of our business and implementation of our growth strategies, including our ability to accommodate additional game players and advertising clients in the future, depend upon the performance and reliability of the Internet infrastructure and fixed telecommunications networks in China.*

Almost all access to the Internet in China is maintained through state-owned telecommunications operators under the administrative control and regulatory supervision of the Ministry of Industry and Information Technology, or MIIT. We rely on this infrastructure to provide data communications capacity, primarily through local telecommunications lines. Although the PRC government has announced plans to develop the national information infrastructure, this infrastructure may not be developed as planned or at all. In addition, we will have no access to alternative networks and services, on a timely basis if at all, in the event of any infrastructure disruption or failure. The Internet infrastructure in China may not support the demands necessary for continued growth in Internet usage.

*Most of our revenues generated by the 17173 Business are from online advertising. The online advertising market includes many uncertainties, which could cause our revenues from the 17173 Business to fail to grow or to decline.*

The 17173 Business, which derives revenue primarily from providing advertising services on the 17173.com Website, had online advertising revenues of \$50.0 million and IVAS revenues of \$5.4 million for the year ended December 31, 2013, together representing 7.5% of our total revenues for the year. Our ability to maintain or grow revenues from the 17173 Business may be adversely affected by any of the following risk factors:

- The online advertising market is new and rapidly evolving, particularly in China. As a result, many of our current and potential advertising clients have limited experience using the Internet for advertising purposes and historically have not devoted a significant portion of their advertising budgets to Internet-based advertising;
- Changes in government policy could restrict or curtail our online advertising services;
- Advertising clients may adopt new methods and strategies other than online advertising to promote their brands, which would have an adverse impact on our advertising revenues; and
- The acceptance of the Internet as a medium for advertising depends on the development of a measurement standard. No standards for the measurement of the effectiveness of online advertising have been widely accepted. Industry-wide standards may not develop sufficiently to support the Internet as an effective advertising medium. If these standards do not develop, advertisers may choose not to advertise on the Internet in general, or through our Websites.

In addition, our ability to generate and maintain significant online advertising revenues will also depend upon:

- the development of a large base of users possessing demographic characteristics attractive to advertising clients;
- the acceptance of online advertisements as an effective method of business marketing;
- the effectiveness of our advertising delivery, tracking and reporting systems;
- the extent of resistance from existing or potential customers to online advertising prices; and
- the development of new formats for online advertising, such as streaming video.

*The expansion of Internet advertisement blocking software may result in a decrease in advertising revenues.*

The development of Web software that blocks Internet advertisements before they appear on a user's screen may hinder the growth of online advertising. The expansion of advertisement blocking on the Internet may decrease our revenues from the 17173 Business because, when an advertisement is blocked, it is not downloaded from the server, which means that it will not be tracked as a delivered advertisement. In addition, advertisers may choose not to advertise on the Internet or on our 17173.com Website because of the use by third parties of Internet advertisement blocking software.

*Our cinema advertising business has generated losses through 2013 and we may not be able to maintain or expand the revenues that we receive from cinema advertising services.*

Our cinema advertising business generates revenues through contracts that we enter into with advertisers to place their advertisements in pre-film advertising slots in movie theatres, and generated losses through 2013. We receive the cinema advertising rights for such pre-film advertising slots under contracts with various theatres and film production companies. We cannot assure you that we will be able to develop, maintain or expand the types of relationships with movie theatres and film production companies that will permit us to receive or preserve our existing rights or obtain any additional rights to pre-movie advertisement slots. Any failure to develop, maintain or expand such relationships could prevent us from increasing our cinema advertising revenues, could cause the business to generate losses and also could result in a decrease in our cinema advertising revenues.



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*We incur additional costs and face significant risks when we operate, license, or jointly operate with third-party joint operators, our games outside of China and seek to expand our operations to select markets. If we fail to manage these risks, our growth and business prospects could be adversely affected.*

We currently license some of our games, including TLBB, to, and jointly operate DDTank and Wartune with, third-party operators in regions and countries outside of China. We plan to continue to license and jointly operate these games and other future games in these and other overseas markets. We have expanded our direct game operations to select markets, such as the United States, Malaysia and India, and expect to expand our direct game operations (through local wholly-owned subsidiaries) to other overseas markets. Identifying appropriate overseas markets, negotiating with potential third-party licensees or joint operators and managing our relationships with our licensees and joint operators all require substantial management effort and skills and the incurrence of significant expenses. Licensing our games and operating them overseas directly or jointly with third-party joint operators also require translation of our games into the local languages of the overseas markets in which we plan to license or operate, and may require customization as well, both of which require significant additional expense. There are additional risks associated with the licensing or direct or joint operation of our games overseas, including:

- difficulties in identifying and maintaining good relationships with licensees or joint operators who are knowledgeable about, and can effectively distribute and operate our games in, overseas markets;
- difficulties and costs relating to compliance with the different legal requirements and commercial terms in the overseas markets in which we license or directly or jointly operate our games, such as game export regulatory procedures, taxes and other restrictions and expenses;
- difficulties in maintaining the reputation of our company and our games when our games are operated by licensees or joint operators in overseas markets pursuant to their own standards;
- changes in the political, regulatory or economic conditions in a foreign country or region, or public policies toward online games;
- exposure to different regulatory systems governing the protection of intellectual property and the regulation of online games, the Internet and the export of technology;
- difficulties in verifying revenues generated from our games by our licensees for purposes of determining royalties payable to us;
- inherent difficulties and delays in contract enforcement and collection of receivables through the use of foreign legal systems;
- difficulties in protecting our intellectual property;
- difficulties in managing our overseas employees when we operate our games directly overseas;
- the risk that the regulatory authorities in foreign countries or administrative regions may impose withholding taxes, or place restrictions on repatriation of our profits; and
- fluctuations in currency exchange rates.

If we are unable to manage these risks effectively, our ability to license or operate our games overseas either directly or jointly with third-party joint operators may be impaired.

*Rapid technological changes may increase our game development costs.*

The online game industry is evolving rapidly, so we need to anticipate new technologies and evaluate their possible market acceptance. In addition, government authorities or industry organizations may adopt new standards that apply to game development. Any new technologies and new standards may require increases in expenditures for MMOG, Web games or mobile game development and operations, and we will need to adapt our business to cope with the changes and support these new services to be successful. If we fall behind in adopting new technologies or standards, our existing games may lose popularity, and our newly developed games may not be well received in the marketplace.





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*The proliferation of “cheating” programs and scam offers that seek to exploit our games and players harms the game-playing experience and may lead players to stop playing our games.*

Unrelated third parties have developed, and may continue to develop, “cheating” programs that enable players to exploit our games, play them in an automated way or obtain unfair advantages over other players who play fairly. These programs harm the experience of players who play fairly and may disrupt the economics of our games. In addition, unrelated third parties may attempt to scam our players with fake offers for virtual goods. We need to devote significant resources to discover, disable and prevent such programs and activities, and if we are unable to do so quickly our operations may be disrupted, our reputation may be damaged and players may stop playing our games. This may lead to lost revenue and increased costs for us to develop technological measures to combat such programs and activities.

*Our business may be harmed if our games are not featured in a sufficient number of Internet cafés in China*

A substantial number of game players access our games through Internet cafés in China. Due to limited hardware capacity, Internet cafés generally feature a limited number of games on their computers. We thus compete with a growing number of other online game operators to ensure that our games are featured on these computers. This competition is intensified by restrictions by the Ministry of Culture, or MOC, on the establishment of new Internet cafés and on the total number of Internet cafés nationwide. It is necessary for us to maintain good relationships with Internet café operators, require our distributors to maintain a sales presence in a large number of Internet cafés, and conduct periodical promotional activities in select Internet cafés and other general sales and marketing efforts to ensure that our games are featured in a sufficient number of Internet cafés. If we fail to maintain good relationships with Internet café operators, or if we and/or our distributors fail to successfully persuade Internet cafés to feature our games, our revenues may be adversely affected.

*We may fail to maintain a stable and efficient distribution network for our virtual prepaid game cards.*

Online payment systems in China are in a developmental stage and are not as widely available to or accepted by consumers in China as they are in the United States. We mainly rely on a distribution network composed of third-party distributors for sales of our virtual prepaid game cards to our game players. As a result, our revenues could be adversely affected by under-performance by our distributors, such as a failure to meet minimum sales or penetration targets or to establish an extensive online retail network. We generally sign one-year agreements with our distributors. We may not continue to maintain favorable relationships with them. In addition, our distributors may violate our distribution agreements. Such violations may include, among other things, their:

- failure to maintain minimum price levels for our prepaid game cards in accordance with our distribution agreements;
- failure to properly promote our MMOGs in local Internet cafés and other important outlets, or cooperate with our sales and marketing team’s efforts in their designated territories; and
- selling our virtual prepaid game cards outside their designated territories.

In the past, some of our distributors have failed to carry out their obligations in accordance with our distribution agreements with them, which resulted in our termination of our distribution relationships with them. If we decide to penalize, suspend or terminate our distributors for acting in violation of our distribution agreements, or if the distributors fail to address violations committed by any of their retail outlets in a timely manner, our ability to effectively sell our prepaid game cards in any given territory could be negatively impacted, which would adversely affect our revenues.

Commencing in October 2013, we discontinued sales discounts, and decreased rebate rates, that we had previously offered to our prepaid game card distributors, while increasing our direct sales of game points to our game players through our own online sales platform. See “Information on the Company—Sales and Distribution” in Item 4 and “Operating And Financial Review And Prospects—Revenue Collection—Online Game Revenues—MMOG operations” in Item 5. Such discontinuation and decrease may disincentivize our distributors from effectively selling our prepaid game cards, which would adversely affect our revenues.

*We could be liable for breaches in the security of our online payment platforms and those of third parties with whom we transact business, and any such breaches could cause our customers to lose confidence in the integrity of the payment systems that we use.*

Currently, we sell a substantial portion of our virtual prepaid game cards and game points to our game players through third-party online payment platforms. In these online transactions, secure transmission of confidential information, such as customers’ credit card numbers and expiration dates, personal information and billing addresses, over public networks is essential if we are to maintain our consumers’ confidence in us. In addition, we expect that an increasing amount of our sales will be conducted over the Internet as a result of the growing use of online payment systems. As a result, the risk of associated online crime will increase. Our current security measures and those of the third parties with whom we transact business may not be adequate. We must be prepared to increase our security measures and efforts so that our game players have confidence in the reliability of the online payment systems that we use, which will require us to incur additional expense. Such increased security measures may still not make our online payment systems completely safe. In addition, we do not have control over the security measures of our third-party online payment vendors. Breaches in the security of online payment systems that we use could expose us to litigation and liability for failing to secure confidential customer information, and could harm our reputation, ability to attract customers and ability to encourage customers to purchase virtual items.



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*We rely on advertising agencies to sell the online advertising services of the 17173 Business. If current trends of consolidation of advertising agencies in the Chinese market continue, the bargaining power of the large advertising agencies resulting from such consolidation may permit them to require that we pay higher sales rebates, which would adversely affect our gross margin.*

Most of the online advertising services of the 17173 Business are distributed by, and most of the online advertising revenues of the 17173 Business are derived from, advertising agencies. In 2013, for example, we engaged five advertising agencies, which contributed approximately 84% of the online advertising revenues of the 17173 Business. In consideration for these agencies' services, we are required to pay certain percentages of revenues as sales rebates. If the online advertising market is consolidated and effectively controlled by a small number of large advertising agencies, such advertising agencies may be in a position to demand higher sales rebates based on increased bargaining power, which could negatively affect our online advertising growth as we book our online advertising revenue net of our sales rebates to advertising agencies.

*As we grow our business and expand into new types of games and platform channels, we will need to hire a significant number of new employees. If we are unable to attract a sufficient number of qualified new employees, our business prospects may be adversely affected.*

As we grow our business and expand into mobile games, the platform channel business and international markets, we will need to increase the number of our employees, including senior-level executives, experienced project managers, game development personnel and game operations professionals. The number of our employees increased 35.3% between the end of 2012 and the end of 2013. Our industry in China is characterized by high demand and intense competition for talent, particularly for game developers and related technical personnel, and we may not be able to attract a sufficient number of additional qualified employees to meet the growth of our business, which would adversely affect our growth strategy and our business prospects.

*We may be exposed to infringement or misappropriation claims by third parties, which, if determined adversely to us, could subject us to significant liabilities and other costs.*

Our success depends largely on our ability to use and develop our technology and know-how without infringing the intellectual property rights of third parties. We cannot assure you that third parties will not assert intellectual property claims against us. We are subject to additional risks if entities licensing to us intellectual property, including, for example, game source codes, do not have adequate rights in any such licensed materials. The validity and scope of claims relating to the intellectual property of game development and technology involve complex scientific, legal and factual questions and analyses and, therefore, tend to be uncertain. If third parties assert copyright or patent infringement or violation of other intellectual property rights against us, we will have to defend ourselves in litigation or administrative proceedings, which can be both costly and time consuming and may significantly divert the efforts and resources of our technical and management personnel. An adverse determination or settlement in any such litigation or proceedings to which we may become a party could subject us to significant liability to third parties, or require us to seek licenses from third parties, pay ongoing royalties, or redesign our games or subject us to injunctions prohibiting the development and operation of our games.

In addition, in the case of our Web games, our potential exposure to litigation alleging that our games infringe the intellectual property of others may extend to potential claims against the third-party joint operators of our games. We typically agree in our agreements with joint operators to indemnify the joint operators against claims of infringement relating to our games. As a result, we may have to defend our joint operators with respect to any allegations against them with respect to infringement by our games, which could be both costly and time consuming.

*We may need to incur significant expenses to enforce our proprietary rights, and if we are unable to protect such rights, our competitive position and financial performance could be harmed.*

We regard our intellectual property and proprietary rights as critical to our success. In particular, we have spent a significant amount of time and resources in developing our current games and our pipeline games. Our ability to protect our proprietary rights in connection with our games is critical for their success and our overall financial performance. While we have registered software in China for copyright protection and have taken various measures to protect our source codes, such measures may not be sufficient to protect our proprietary information and intellectual property. Intellectual property rights and confidentiality protection in China may not be as effective as they are in the United States and other developed countries. Policing unauthorized use of proprietary technology is difficult and expensive. In addition, while we have registered some trademarks relating to our games in the PRC and other jurisdictions, and have applied for additional registrations of trademarks, in some instances we may not succeed in obtaining registration of trademarks that we have applied in different languages, such as English. We cannot assure that these pending or future trademark applications will be approved. Any failure to register trademarks in any country or region may limit our ability to protect our rights in such country or region under relevant trademark laws, and we may even need to change the name or the relevant trademark in certain cases, which may adversely affect our branding and marketing efforts.



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Despite our efforts to protect our intellectual property, online game developers may copy our ideas and designs, and other third parties may infringe our intellectual property rights. For example, certain third parties have misappropriated the source codes of previous versions of TLBB and have set up unauthorized servers in China and elsewhere to operate TLBB to compete with us. Although in response we have taken measures to enforce our intellectual property rights, such measures may not be successful in eliminating these unauthorized servers. The existence of unauthorized servers may attract game players away from our games and may result in decreases in our revenues. Litigation relating to intellectual property rights may result in substantial costs to us and diversion of resources and management attention away from our business, and may not be successful. In addition, our ideas and certain of our designs, if not fixed in a tangible form of expression or registered with the appropriate PRC authorities, may not be protected by patents or other intellectual property rights. As a result, we may be limited in our ability to assert intellectual property rights against online game developers who independently develop ideas and designs that compete with us.

*We may not have exclusive rights to trademarks, designs and technologies that are crucial to our business.*

We have applied for initial registrations in the PRC and overseas, and/or changes in registrations relating to transfers of our key trademarks in the PRC, including ChangYou.com, cyou.com, 7Road, TLBB, TL logos, Blade Online, DMD, DDTank, Wartune, DPCQ, 17173 and the corresponding Chinese versions of the marks, so as to establish and protect our exclusive rights to these trademarks. We have succeeded in registering the trademarks ChangYou.com, cyou.com, 7Road, TLBB, TL logos, DMD, DDTank and 17173 in the PRC under certain classes. The applications for initial registration, and/or changes in registrations relating to transfers, of other marks and/or of some of these marks under other classes are still under examination by the Trademark Office of the State Administration for Industry & Commerce of the PRC, or the SAIC, and relevant authorities overseas. We have applied for patents relating to the design of our games and to technology intended to enhance the functionalities of our games. We have succeeded in registering 5 patents and our other patent applications are under examination by the State Intellectual Property Office of the PRC. Approvals of our initial trademark registration applications, and/or of changes in registrations relating to such transfers, or of our patent applications, are subject to determinations by the Trademark Office of the SAIC, the State Intellectual Property Office of the PRC and relevant authorities overseas that there are no prior rights in the applicable territory. We cannot assure that these applications will be approved. Any rejection of these applications could adversely affect our rights to the affected marks, designs and technologies. In addition, even if these applications are approved, we cannot assure you that any registered trademark or issued patent will be sufficient in scope to provide adequate protection of our rights.

*Breaches in the security of our server network could cause disruptions in our service, facilitate piracy of our intellectual property, or compromise confidential information of our game players.*

We store on our servers and transmit over the Internet considerable and continually increasing amounts of data, much of which is essential to the operation of our business or is highly confidential information concerning our business and our game players. In addition, the expansion of our business to include Web and mobile games and our need to comply with PRC regulations requiring real-name registration of our game players are likely to cause the amount of personal data concerning our game players that is transmitted over our networks to increase over time. Any breaches of our network by hackers could cause severe disruptions in our service, allow piracy of the source code used in the operation of our games and allow pirated versions of our games to enter the marketplace, or result in the release of confidential personal or financial information of our game players, any of which could have an adverse impact on our business, our revenues, and our reputation among game players. In order to minimize the likelihood of such breaches as our business expands and the amount of confidential and sensitive data increases, we expect that we will need to expend considerable resources to maintain and enhance the effectiveness of our security systems.

*We may be subject to, and may expend significant resources in defending against, claims regarding the content and services we provide over our Websites.*

As our services may be used to download and distribute information to others, there is a risk that claims may be made against us for defamation, negligence, copyright or trademark infringement or based on the nature and content of such information. Furthermore, we could be subject to claims related to the online activities of our visitors and incur significant costs in our defense. In the past, claims regarding the nature and content of information that was posted online by visitors have been made in the United States against companies that provide online services. We could be exposed to liability for the selection of listings that may be accessible through our Websites or through content and materials that our visitors may post in classifieds, message boards, chat rooms or other interactive services. If any information provided through our services contains errors, third parties may make claims against us for losses incurred in reliance on the information.

We do not carry any liability insurance against of the foregoing risks.



*We do not have business insurance coverage.*

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

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

The penetration rate for personal computers in China is significantly lower than it is in the United States and other developed countries. Furthermore, the cost of Internet access in China is still relatively high as compared to other developed countries. The limited use of personal computers in China and the relatively high cost of Internet access may limit the growth of our business. In addition, there may be increases in Internet access fees or telecommunication fees in China. If that happens, the number of our game players may decrease or the growth of our game player base may be adversely impacted. Slow growth of, or a decrease in, the traffic on the 17173.com Website may also cause our advertising clients to reduce their use of our online advertising services, reducing our online advertising revenues.

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

Our business could be adversely affected by the effects of avian flu, SARS, H1N1 or other epidemics or outbreaks. China reported a number of cases of SARS in 2003, which resulted in the closure by the PRC government of many businesses to prevent the transmission of the disease. Similarly, there were many businesses in China that were affected by the outbreak of the H1N1 virus in 2009, and in recent years there have been reports of occurrences of avian flu in various parts of China, including a few confirmed human cases and deaths. Any prolonged recurrence of avian flu, SARS, H1N1 or other adverse public health developments in China may have an adverse effect on our business operations. Adverse effects could include illness and loss of our management and key employees, as well as temporary closure of our offices and related other businesses, such as server operations, upon which we rely, and a decrease in the number of our game players. Such loss of management and key employees or closures would severely disrupt our business operations. We have not adopted any written preventive measures or contingency plans to combat any future outbreak of avian flu, SARS, H1N1 or any other epidemic. In addition, other major natural disasters may also adversely affect our business by, for example, causing disruptions of the Internet network or otherwise affecting access to our games.

### ***Risks Related to Our Corporate Structure and PRC Law and Regulations***

*If the PRC government determines that the VIE structure for operating our business does not comply with applicable PRC government restrictions on foreign investment in the online game industry and the online advertisement industry, we could face severe penalties.*

Various regulations in China currently restrict foreign-invested entities from engaging in value-added telecommunication services, which are defined by PRC authorities to include operating online games and providing online advertisements. Because of these restrictions, we operate certain aspects of our game business in the PRC through our variable interest entities, or VIEs, which include Beijing Gamease Age Digital Technology Co., Ltd., or Gamease, Shenzhen 7Road Technology Co., Ltd., or Shenzhen 7Road, Beijing Guanyou Gamespace Digital Technology Co., Ltd., or Guanyou Gamespace, and Shanghai ICE Information Technology Co., Ltd., or Shanghai ICE. The current shareholders of Gamease and Guanyou Gamespace are Tao Wang, our Chief Executive Officer, and Dewen Chen, our President, who hold 60% and 40%, respectively, of each of these entities. The equity interests in Shenzhen 7Road are owned 100% by our VIE Gamease, which is a PRC company. The equity interests in Shanghai ICE are owned by two of our employees, Runa Pi and Rong Qi, each of whom holds 50%. Each of the nominee shareholders of these VIEs is either a PRC citizen or a PRC company. Through a series of contractual arrangements, Gamease is effectively controlled by our indirect PRC subsidiary Beijing AmazGame Age Internet Technology Co., Ltd., or AmazGame; Shenzhen 7Road is effectively controlled by our indirect PRC subsidiary Shenzhen 7Road Network Technologies Co., Ltd., or 7Road Technology; Guanyou Gamespace is effectively controlled by our indirect PRC subsidiary Beijing Changyou Gamespace Software Technology Co., Ltd., or Gamespace; and Shanghai ICE is effectively controlled by our indirect PRC subsidiary ICE Information Technology (Shanghai) Co., Ltd, or ICE Information. For details of these contractual arrangements, see "Related Party Transactions" in Item 7 of this annual report.





The MIIT issued a circular in 2006 that emphasizes restrictions on foreign investment in value-added telecommunications businesses. In addition, a notice jointly issued in 2009 by the State Administration of Press, Publication, Radio, Film and Television, or the SAPPRFT, the National Copyright Administration, and the National Office of Combating Pornography and Illegal Publications states that foreign investors are not permitted to invest in online game operating businesses in China or to exercise control over or participate in the operation of such businesses through indirect means. Due to a lack of interpretative materials from the relevant PRC authorities, there are uncertainties regarding whether PRC authorities would consider our corporate structure and contractual arrangements to be a kind of foreign investment in value-added telecommunications services or online game operation businesses. While we are not aware of any online game companies which use the same or similar contractual arrangements as ours having been penalized or ordered to terminate operations by PRC authorities claiming that the arrangements constituted foreign investment in value-added telecommunication services or a kind of control over or participation in the operation of online game operating businesses through indirect means, it is unclear whether and how the various regulations of the PRC authorities might be interpreted or implemented in the future. For a detailed discussion of PRC regulations, notices and circulars with respect to such restrictions, see “PRC Regulation—Regulation of Telecommunication Services—Restrictions on Foreign Ownership of Value-Added Telecommunication Services” and “PRC Regulation—Online Games and Cultural Products” in Item 4 of this annual report.

In addition, under the *Notice of the General Office of the State Council on Establishing the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors*, or Circular No. 6, promulgated by the State Council of the PRC, or the State Council, on February 3, 2011 and the *Rules of Ministry of Commerce on Implementation of Security Review System of Mergers and Acquisitions of Domestic Enterprises by Foreign Investors*, or the MOFCOM Security Review Rules, promulgated by the Ministry of Commerce, or MOFCOM, in August, 2011 to implement Circular No. 6, a security review is required for mergers and acquisitions by foreign investors having “national defense and security” concerns and mergers and acquisitions by which foreign investors may acquire the “de facto control” of domestic enterprises with “national security” concerns and prohibit foreign investors from bypassing the security review requirement by structuring transactions through proxies, trusts, indirect investments, leases, loans, control through contractual arrangements or offshore transactions. As there is no explicit provision or official interpretation stating that the business of 7Road falls into the scope subject to security review, we did not submit for security review the formation of our acquisition of interests in Shenzhen 7Road or the formation of the VIE structure of 7Road. However, these national security review-related regulations are relatively new and there is a lack of clear statutory interpretation regarding the implementation of the rules and PRC authorities may interpret these regulations to mean that such transactions should have been submitted for review. Moreover, various media sources reported in 2011 that the China Securities Regulatory Commission, or CSRC, had prepared a report for the State Council, suggesting regulating the use of VIE structures, such as ours, in the context of foreign investment in China and overseas listings. For a discussion of these PRC national security review requirements and media reports, see “PRC Regulation—M&A Regulations and Overseas Listings” in Item 4 of this annual report.

If we were found to be in violation of any existing or future PRC law or regulations relating to foreign ownership of value-added telecommunications businesses and security reviews of foreign investments in such businesses, including online games businesses, regulatory authorities with jurisdiction over the operation of our business would have broad discretion in dealing with such a violation, including levying fines, confiscating our income, revoking the business or operating licenses of PRC subsidiaries and/or VIEs, requiring us to restructure our ownership structure or operations, requiring us to discontinue or divest ourselves of all or any portion of our operations or assets, restricting our right to collect revenues, blocking our Websites, or imposing additional conditions or requirements with which we may not be able to comply. Any of these actions could cause significant disruption to our business operations and have an adverse impact on our business, financial condition and results of operations. Further, if changes were required to be made to our ownership structure, our ability to consolidate our VIEs could be adversely affected.

*Our contractual arrangements with our VIEs and their shareholders may not be as effective in providing control over our VIEs as direct ownership of the VIEs and the shareholders of our VIEs may have conflicts of interest with us or with each other.*

We have no ownership interest in Gamease, Shenzhen 7Road, Guanyou Gamespace, or Shanghai ICE, and we conduct most of our operations and generate substantially all of our revenues through contractual arrangements that our indirect subsidiaries AmazGame, 7Road Technology, Gamespace and ICE Information entered into with Gamease, Shenzhen 7Road, Guanyou Gamespace, Shanghai ICE, respectively, and their shareholders. Such contractual arrangements are designed to provide us with effective control over Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE. See “Related Party Transactions” in Item 7 of this annual report for a description of these contractual arrangements. We depend on Gamease, Shenzhen 7Road, Guanyou Gamespace, and Shanghai ICE to hold and maintain certain licenses and permits necessary for our online game business and the 17173 Business. Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE collectively own all of the necessary intellectual property, facilities and other assets relating to the operation of our online games and the 17173 Business, and employ personnel for the operations and distribution of our games and the operation of the 17173 business that are not owned or employed directly by our subsidiaries.



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These contractual arrangements may not be as effective in providing us with control over Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE as direct ownership. For example, if we had direct ownership of Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, we would be able to exercise our rights as a shareholder to effect changes in their boards of directors, which in turn could effect changes at the management level. Due to our VIE structure, we have to rely on contractual rights to effect control and management of Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, which exposes us to the risk of potential breach of contract by the shareholders of Gamease, Shenzhen 7Road, Guanyou Gamespace, and Shanghai ICE. In addition, as each of Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE is jointly owned by its respective shareholders, it may be difficult for us to change our corporate structure if such shareholders refuse to cooperate with us. Furthermore, if the shareholders of any of our VIEs were involved in proceedings that had an adverse impact on their shareholder interests in such VIE or on our ability to enforce relevant contracts related to the VIE structure, our business would be adversely affected.

The shareholders of Gamease, Shenzhen 7Road, Guanyou Gamespace or Shanghai ICE may breach, or cause Gamease, Shenzhen 7Road, Guanyou Gamespace or Shanghai ICE to breach, the VIE contracts for a number of reasons. For example, their interests as shareholders of Gamease, Shenzhen 7Road, Guanyou Gamespace or Shanghai ICE and the interests of our company may conflict and we may fail to resolve such conflicts; the shareholders may believe that breaching the contracts will lead to greater economic benefit for them; or the shareholders may otherwise act in bad faith. If any of the foregoing were to happen, we might have to rely on legal or arbitral proceedings to enforce our contractual rights. In addition, disputes may arise among the shareholders of any of our VIEs with respect to their ownership of such VIE which could lead them to breach their agreements with us. Such arbitral and legal proceedings and disputes may cost us substantial financial and other resources, and result in disruption of our business, and the outcome might not be in our favor. For example, a PRC court or arbitration panel could conclude that our VIE contracts violate PRC law or are otherwise unenforceable. If the contractual arrangements with any of our VIEs were found by PRC authorities with appropriate jurisdiction to be unenforceable, we could lose our ability to consolidate such VIE's results of operations, assets and liabilities in our consolidated financial statements and/or to transfer the revenues of such VIE to our corresponding PRC subsidiary. In addition, such a finding of unenforceability by PRC authorities could cause more than 75% of our gross income or more than 50% of our assets to be passive in the year that this finding was made or in subsequent years, which could cause us to be classified as a passive foreign investment company, or PFIC. See "We might be classified as a passive foreign investment company, which could result in adverse U.S. federal income tax consequences to U.S. holders of our ADSs or Class A ordinary shares."

Under the contractual arrangements with our VIEs and their shareholders, no shareholder or group of shareholders of any of our VIEs has the ability to unilaterally terminate any of the agreements between the VIEs in which they hold shares and our corresponding PRC subsidiary. However, (i) the shareholders of Gamease, Guanyou Gamespace and Shanghai ICE have a termination right under the loan agreements if our corresponding PRC subsidiary engages in gross negligence, fraud or other material illegal actions or if our corresponding PRC subsidiary existence is terminated as a result of bankruptcy, dissolution, or legal process by government authorities and (ii) the shareholders of our VIEs have a termination right under the equity purchase right agreements if the corresponding VIE's existence is terminated as a result of bankruptcy, dissolution, or legal process by government authorities.

In addition, as all of these contractual arrangements are governed by PRC law and provide for the resolution of disputes through either arbitration or litigation in the PRC, they would be interpreted in accordance with PRC law and any disputes would be resolved in accordance with PRC legal procedures. We would have to rely for enforcement on legal remedies under PRC law, including specific performance, injunctive relief or damages, which might not be effective. For example, if we sought to enforce the equity interest purchase right agreements for the transfer of equity interests in any of our VIEs, if the transferee was a foreign company the transfer would be subject to approval by governmental authorities such as the MIIT and the MOFCOM, and the transferee would be required to comply with various requirements, including qualification and maximum foreign shareholding percentage requirements. As these governmental authorities have wide discretion in granting such approvals, we could fail to obtain such approval. In addition, our VIE contracts might not be enforceable in China if PRC governmental authorities or courts took the view that such contracts contravened PRC law or were otherwise not enforceable for public policy reasons.

Furthermore, the legal environment in the PRC is not as developed as in other jurisdictions, such as the United States. As a result, uncertainties in the PRC legal system could further limit our ability to enforce these contractual arrangements. In the event we were unable to enforce these contractual arrangements, we would not be able to exert effective control over Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, and our ability to conduct our business, and our financial condition and results of operations, would be severely adversely affected.



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*Our contractual arrangements with our VIEs may result in adverse tax consequences to us.*

Under PRC law and regulations, arrangements and transactions among related parties may be subject to audit or challenge by PRC tax authorities. We could face adverse tax consequences if PRC tax authorities determined that our contractual arrangements with any of Gamease, Shenzhen 7Road, Guanyou Gamespace or Shanghai ICE were not made on an arm's length basis and adjust our income and expenses for PRC tax purposes in the form of a transfer pricing adjustment. A transfer pricing adjustment could result in a reduction, for PRC tax purposes, of adjustments recorded by any of our VIEs, which could adversely affect us by (i) increasing the tax liability of such VIE without reducing the tax liability of our corresponding PRC subsidiary, which could further result in interest and penalties being levied on us for underpaid taxes or (ii) limiting such VIE's ability to maintain preferential tax treatments and other financial incentives. In addition, if for any reason we needed to cause the transfer of any of the shareholders' shares in any of our VIEs to a different nominee shareholder (such as if, for example, one of such shareholders is no longer employed by us), we might be required to pay individual income tax, on behalf of the transferring shareholder, on any gain deemed to have been realized by such shareholder on such transfer.

*We may lose the ability to use and enjoy assets held by any of our VIEs that are important to the operation of our business if such VIE declares bankruptcy or becomes subject to a dissolution or liquidation proceeding.*

Each of our VIEs holds assets that are critical to our business operations, such as our core intellectual property, licenses and permits, and/or joint operation agreements relating to our games and game operations. Although the equity interest purchase right agreements among our wholly foreign-owned entities, or WFOEs, our VIEs and the shareholders of our VIEs contain terms that specifically obligate the shareholders of our VIEs to ensure the valid existence of our VIEs, in the event the shareholders breached this obligation and voluntarily liquidated our VIEs, or if any of our VIEs declared bankruptcy and all or part of its assets became subject to liens or rights of third-party creditors, we might be unable to continue some or all of our business operations. Furthermore, if any of our VIEs were to undergo a voluntary or involuntary liquidation proceeding, its shareholders or unrelated third-party creditors might claim rights to some or all of such VIE's assets and their rights could be senior to our rights under the VIE contracts, thereby hindering our ability to operate our business.

*Substantially all of our revenues are generated through Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, our VIEs, and we rely on payments made by Gamease, Shenzhen 7Road, Guanyou Gamespace, Shanghai ICE to AmazGame, 7Road Technology, Gamespace and ICE Information, our subsidiaries, pursuant to contractual arrangements to transfer any such revenues to AmazGame, 7Road Technology, Gamespace and ICE Information. Any restriction on such payments and any increase in the amount of PRC taxes applicable to such payments may adversely affect our business and our ability to pay dividends to our shareholders and ADS holders.*

We conduct substantially all of our operations through Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, our VIEs, which generate substantially all of our revenues. As our VIEs are not owned by our subsidiaries, they are not able to make dividend payments to our subsidiaries. Instead, each of AmazGame, 7Road Technology, Gamespace and ICE Information, our subsidiaries in China, entered into a number of contracts with its corresponding VIE, pursuant to which the VIE pays the PRC subsidiary for certain services that the PRC subsidiary provides to the VIE. However, depending on the nature of services provided, certain of these payments are subject to PRC taxes, including business taxes and value-added tax, or VAT, which effectively reduce the amount that we receive from the VIEs. The PRC government might impose restrictions on such payments or change the tax rates applicable to such payments. Any such restrictions on such payment or increases in the applicable tax rates could limit our ability to receive payments from the VIEs or limit the amount of such payments, and could in turn adversely affect our business, our net income and our ability to pay dividends to our shareholders and ADS holders.

*We operate some of our existing games, and plan to operate certain of our pipeline and future games, with Internet publishing numbers that we obtained through unrelated third-party electronic publishing entities. If the SAPPRFT challenges the commercial operation of any of our games that is operated with an Internet publishing number obtained through a third-party publishing entity, we may be subject to various penalties, including restrictions on our operations.*

Under PRC regulations issued by the SAPPRFT and the MIIT relating to the regulation of online publication, an Internet publishing license is required under PRC regulations for online game operators, and a publishing number obtained under such a license is required for each game in operation and publicly available in the PRC. We publish certain of our existing games with publishing numbers obtained through third-party licensed electronic publishing entities. Our VIE Shanghai ICE is still in the process of applying for an Internet publishing license and our VIE Shenzhen 7Road intends to continue to publish certain of its pipeline and future games with publishing numbers obtained through third parties. See "Regulations—Online Games and Cultural Products" in Item 4 of this annual report. Current PRC regulations are not clear as to the consequence of obtaining publishing numbers through third-party electronic publishing entities. Our past and expected future practices might be challenged by the SAPPRFT, which could subject us to various penalties, including fines, confiscation of publishing equipment and the revenues generated from the publishing activities, the revocation of our business license, or the forced discontinuation of or restrictions on our operations.





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*If we are found to be in violation of current or future PRC law and regulations regarding Internet-related services and telecom-related activities, we could be subject to severe penalties.*

The PRC government has enacted regulations that apply to Internet-related services and telecom-related activities. While many aspects of these regulations remain unclear, they purport to limit and require licensing of various aspects of the provision of Internet information and content, online games, and online advertising services.

Under regulations issued by the SAPPRFT, Websites authorized to disseminate news must apply to the SAPPRFT to obtain a Permit for the Network Transmission of Audiovisual Programs in order to disseminate streaming video online. Under additional SAPPRFT regulations, the business of providing public program searching and watching services through the Internet to the public is classified as an Internet audio-video program service for which a Permit for the Network Transmission of Audiovisual Programs is required. Our online video services offered on the 17173.com Website are operated by Guanyou Gamespace through a permit held by Beijing Sohu Internet Information Service Co., Ltd, which is a VIE of Sohu, and Guanyou Gamespace has not yet been granted such a permit directly. If the video services conducted by Guanyou Gamespace are later challenged by the SAPPRFT, we may be subject to severe penalties, including fines, or the suspension of our video services or even our operations. If we are ordered to suspend the video services provided under 17173.com Website, our user traffic will be reduced and therefore our revenues derived from online advertising will be negatively affected. In addition, Guanyou Gamespace is in the process of renewing its ICP license and Online Culture Operating Permit to include the 17173 Business. If Guanyou Gamespace is unable to obtain such renewals, we may not be allowed to continue the operation of the 17173 Business or be subject to severe penalties.

In addition, the PRC government may promulgate new laws or regulations at any time. If current or future laws or regulations regarding Internet-related activities are interpreted to be inconsistent with our ownership structure and/or our business operations, our business could be severely impaired and we could be subject to severe penalties.

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

The PRC government has adopted regulations governing Internet access and the distribution of news and other information over the Internet. Under these regulations, Internet content providers and Internet publishers are prohibited from posting or displaying over the Internet any content that, among other things, violates PRC law and regulations, impairs the national dignity of China, or is obscene, superstitious, fraudulent or defamatory. When Internet content providers and Internet publishers, including online game operators, find that information falling within the above scope is transmitted on their Websites or is stored in their electronic bulletin service systems, they are required to terminate the transmission of such information or delete such information immediately, keep records, and report to relevant authorities. Failure to comply with these requirements could result in the revocation of our ICP license and other required licenses and the closure of our Websites. Internet content providers may also be held liable for prohibited information displayed on, retrieved from or linked to their Websites.

In addition, the MIIT has published regulations that subject Internet content providers to potential liability for the actions of game players and others using their Websites, including liability for violations of PRC law prohibiting the dissemination of content deemed to be socially destabilizing.

As these regulations are subject to interpretation by the relevant authorities, it is not possible for us to determine in all cases the type of content that could result in liability for us as an MMOG developer and operator, a developer and operator of Web and mobile games and an operator of the 17173 Business. In addition, we may not be able to control or restrict the content of other Internet content providers linked to or accessible through our Websites, or content generated or placed on our Websites by our game players, despite our attempt to monitor such content. To the extent that regulatory authorities find any portion of our content objectionable, they may require us to curtail our games, which may reduce our game player base, the amount of time our games are played or the purchases of virtual items.

*We may be subject to the PRC government's ongoing crackdown on Internet pornographic content.*

The PRC government has stringent regulations on online pornographic information and has launched several crackdowns on Internet pornography. Regulations jointly issued by the MIIT and three other government authorities jointly provide for rewards of up to RMB10,000 to Internet users who report Websites that feature pornography and the MIIT established a committee to review such reports to determine an appropriate award. We have not, to date, received any penalty from the PRC government in this regard. However, it is possible that content considered pornographic or vulgar by PRC government agencies will appear in the future on Websites or games that we operate. In the event that we are accused by the PRC government of hosting pornographic or vulgar content, our business and reputation could be adversely affected.



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*There are currently no laws or regulations in the PRC governing property rights of virtual assets and therefore it is not clear what liabilities, if any, we may have relating to the loss of virtual assets by our game players.*

In the course of playing our games, some virtual assets, such as game player experience, skills and weaponry, are acquired and accumulated. Such virtual assets can be highly valued by game players and in some cases are traded among game players for real money or assets. In practice, virtual assets can be lost for various reasons, such as data loss caused by delay of network service by a network crash, or by hacking activities. There are currently no PRC law and regulations governing property rights of virtual assets. As a result, it is unclear who the legal owner of virtual assets is and whether the ownership of virtual assets is protected by law. In addition, it is unclear under PRC law and regulations whether an operator of online games such as us would have any liability (whether in contract, tort or otherwise) for loss of such virtual assets by game players. Based on several judgments regarding the liabilities of online game operators for loss of virtual assets by game players, the courts have generally required the online game operators to provide well-developed security systems to protect such virtual assets owned by game players. In the event of a loss of virtual assets, we may be sued by game players and may be held liable for damages.

*Our online game operations may be adversely affected by implementation of anti-fatigue-related regulations.*

The PRC government may decide to adopt more stringent policies to monitor the online game industry as a result of adverse public reaction to perceived addiction to online games, particularly by minors. Eight PRC government authorities, including the SAPPRFT, the Ministry of Education and the MIIT, jointly issued regulations, or the Anti-Fatigue Notice, requiring all Chinese online game operators to adopt an “anti-fatigue system” in an effort to curb addiction to online games by minors. Under the anti-fatigue system, three hours or less of continuous play is defined to be “healthy,” three to five hours is defined to be “fatiguing,” and five hours or more is defined to be “unhealthy.” Game operators are required to reduce the value of game benefits for minor game players by half when those game players reach the “fatiguing” level, and to zero when they reach the “unhealthy” level. In addition, online game players in China are now required to register their identity card numbers before they can play an online game. This system allows game operators to identify which game players are minors. These restrictions could limit our ability to increase our business among minors. If these restrictions were expanded to apply to adult game players in the future, our revenues could be adversely affected.

These eight PRC government authorities subsequently promulgated additional regulations, including a *Notice on Initializing the verification of Real-name Registration for Anti-Fatigue System on Internet Games*, or the Real-name Registration Notice, to strengthen the implementation of the anti-fatigue system and real-name registration. The Real-name Registration Notice’s main focus is to prevent minors from using an adult’s identity to play Internet games and, accordingly, provides stringent punishment for online game operators for not implementing the anti-fatigue and real name registration measures properly and effectively. The most severe punishment contemplated by the Real-name Registration Notice is termination of the operation of the online game if it is found to be in violation of the Anti-Fatigue Notice, the Real-name Registration Notice or the circular entitled *Implementation of Online Game Monitor System of the Guardians of Minors*, or the Monitor System Circular. The Real-name Registration Notice increases our operating risks, as we will be required to spend more resources on the real-name verification and anti-fatigue system, which will lead to an increase in our operating costs. In addition, the amount of time that minors will be able to spend playing online games such as ours will be further limited, which can be expected to lead to a reduction in our revenues. Furthermore, if we are found to be violating these regulations, we may be required to suspend or discontinue our online game operations.

In February 2013, 15 PRC government authorities, including the SAPPRFT, the Ministry of Education, the MOC and the MIIT, jointly issued the *Work Plan for the Integrated Prevention of Minors Online Game Addiction*, or the Work Plan, implementing integrated measures by different authorities to prevent minors from being addicted to online games. Under the Work Plan, the current relevant regulations will be further clarified and additional implementation rules will be issued by relevant authorities. As a result, we may have to impose more stringent limits for minor game players, which may lead to an increase in our operating expenses and a reduction in our revenues from minor game players.

*The PRC government has implemented tight regulation of Internet cafés, which are currently one of the primary places where our games are played. Strict government regulation of Internet cafés could restrict our ability to maintain or increase our revenues and our game player base.*

Internet cafés are one of the primary places where our games are played. In April 2001, the PRC government began tightening its regulation and supervision of Internet cafés. In particular, a large number of Internet cafés without requisite government licenses were closed. In addition, the PRC government imposed capital and facility requirements for the establishment of Internet cafés. The PRC government’s policy encourages the development of a limited number of national and regional Internet café chains and discourages the establishment of independent Internet cafés, and the total number of Internet cafés nationwide is restricted and controlled by the relevant authorities. Governmental authorities may from time to time impose stricter requirements, such as limits on the ages of customers and on hours of operation, among others, as a result of the occurrence or perception of, or media attention on, gang fights, fires and other incidents in or related to Internet cafés. So long as Internet cafés remain as one of the primary places for game players to play our games, a reduction in the number, or any slowdown in the growth, of Internet cafés or restrictions on their operations in China could limit our ability to maintain or increase our revenues and our game player base.



*Restrictions on virtual currency may adversely affect our online game revenues.*

Our online game revenues are collected through the sale of our prepaid cards or online sale of game points. The *Notice on the Reinforcement of the Administration of Internet Cafés and Online Games*, or the Internet Cafés Notice, issued by the MOC in 2007, directs the People's Bank of China, or the PBOC, to strengthen the administration of virtual currency in online games to avoid any adverse impact on the PRC economy and financial system. The Internet Cafés Notice places strict limits on the total amount of virtual currency issued by online game operators in the PRC and the amount purchased by individual users in the PRC, and requires a clear division between virtual transactions and real transactions carried out by way of electronic commerce. The Internet Cafés Notice also provides that virtual currency should only be used to purchase virtual items. In 2009, the MOC and the MOFCOM jointly issued the *Notice on Strengthening the Administration of Online Game Virtual Currency*, or the Virtual Currency Notice. In the Virtual Currency Notice, the MOC and the MOFCOM for the first time defined "virtual currency" as a type of virtual exchange instrument issued by online game operators, purchased directly or indirectly by the game user by exchanging legal currency at a certain exchange rate, saved outside the game programs, stored in servers provided by online game operators in electronic record format and represented by specific numeric units. In addition, the Virtual Currency Notice categorizes companies involved with virtual currency in the PRC as either issuers or trading platforms and prohibits companies from simultaneously operating both as issuers and as trading platforms. One of the Virtual Currency Notice's stated intended objectives is to limit the circulation of virtual currency and thereby reduce concerns that it may impact real world inflation. Specifically, the Virtual Currency Notice requires online game operators to report the total amount of their issued virtual currency on a quarterly basis, and game operators are prohibited from issuing disproportionate amounts of virtual currency in order to generate revenues. In addition, the Virtual Currency Notice reiterates that virtual currency can only be provided to users in exchange for an RMB payment and can only be used to pay for virtual goods and services of the issuers. Online game operators are prohibited from providing lucky draws or lotteries which are conducted on the condition that participants contribute cash or virtual currencies in exchange for game props or virtual currencies, and from providing virtual currency trading services to minors. The Virtual Currency Notice places additional potentially burdensome obligations on online game operators, including a requirement that operators keep transaction data records for no less than 180 days, which means that we must design and operate our databases so that we can maintain users' information for the minimum required period, resulting in higher costs for our online game operations. We must tailor our business model carefully in order to comply with the overall requirements of the Virtual Currency Notice, in a manner which can be expected to result in relatively lower sales of our game coins and an adverse impact on our online game revenue.

*Our business may be adversely affected by public opinion and governmental policies in China as well as in other jurisdictions where we operate our MMOGs and Web games or license our MMOGs and Web games to third parties.*

Currently, most of our game players in China are young males, many of whom are students. Due to a relatively high degree of game player loyalty to MMOGs or Web games, easy access to personal computers and Internet cafés, and the lack of other appealing forms of entertainment in China, many teenagers in China frequently play online games. This may result in these teenagers spending less time on or refraining from other activities, including education, vocational training, sports, and resting, which could result in adverse public reaction and stricter government regulation. For example, the PRC government has promulgated anti-fatigue-related regulations to limit the amount of time minors can play online games.

Adverse public opinion could discourage game players from playing our games, and could result in government regulations that impose additional limitations on the operations of online games as well as game players' access to online games. For example, under the Monitor System Circular online game operators are required to adopt various measures to maintain a system to communicate with the parents of minors playing online games and are required to monitor the activities of minors and suspend the accounts of minors if so requested by their parents. We believe that stricter government regulations, such as regulations imposing stricter age and hour limits, limiting the issuance of virtual currency by online game operators or the amount of virtual currency that can be purchased by an individual game player, and extending anti-fatigue-related regulations to adults, could be implemented in the future. Any such adverse public opinion or tightened government regulations could adversely affect our ability to maintain or increase our revenues.

In addition, the PRC State Administration of Taxation, or the SAT, has announced that it will tax game players on the income derived from the trading of virtual currencies at the rate of 20%. It is currently unclear how the tax will be collected or if there will be any effect on our game players or our business, but collection of such a tax might discourage players who are interested in trading virtual currencies from playing our games, which could reduce our revenues.

Moreover, similar adverse public reaction may arise, and similar government policies may be adopted, in other jurisdictions where we license or operate our games, which could similarly adversely affect our revenues.



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*PRC law and regulations governing the online game industry in China are evolving and subject to future changes. We may fail to obtain or maintain all applicable permits, approvals, registrations and filings.*

The online game industry in China is highly regulated by the PRC government. Various regulatory authorities of the PRC central government, such as the State Council, the MIIT, the SAPPRFT, the MOC and the Ministry of Public Security, are empowered to issue and implement regulations governing various aspects of the online game industry.

We are required to obtain applicable permits, approvals and registrations from, or make necessary filings with, different regulatory authorities in order to operate our online games. For example, as an online game operator in China, we must obtain an ICP license from the MIIT, an Online Cultural Operating Permit from the MOC and an Internet publishing license from the SAPPRFT in order to distribute games through the Internet. Any online game we operate needs to be approved by the SAPPRFT prior to its launch and filed with the MOC within 30 days after its launch. Once a new online game or any upgrade, expansion pack or new version of any existing game is launched, such new game or such upgrade, expansion pack or new version of such existing game must be filed with the MOC and approval must be obtained from the SAPPRFT for online publication. Shenzhen 7Road's current ICP license does not specifically permit the operation of BBS services, and it is unclear whether Shenzhen 7Road is required to have an ICP license that specifically permits such services, as the State Council has issued a decision that such specific approval is not required for an ICP, but local authorities generally continue to require such specific approval for BBS services. If we fail to maintain any of our permits, approvals or registrations, to make any necessary filings, or to apply for and obtain any new permits, approvals or registrations or make any new filings on a timely basis, we may be subject to various penalties, including fines and a requirement that we discontinue or limit our operations.

As the online game industry is at an early stage of development in China, new law and regulations may be adopted from time to time to require additional licenses and permits other than those we currently have, and address new issues that arise. In addition, substantial uncertainties exist regarding the interpretation and implementation of current and any future PRC law and regulations applicable to the online game industry. For example, there is ambiguity as to the division of authority and responsibilities between the SAPPRFT and the MOC with respect to regulating online games and, as a result, there may be overlapping approval requirements with respect to some aspects of our games or our game operations. Furthermore, as mobile games are a new type of online game, there are uncertainties relating to whether a game developer, such as us, which provides mobile games to mobile device users, needs to obtain a separate operating license in addition to the ICP license that it has already obtained. For any mobile games we launch, we may be required to apply for a separate operating license for the mobile applications. Therefore, we may not be able to obtain timely, or at all, required licenses or any other new license required in the future, and we may be found to be in violation of current or future PRC law and regulations, which could impede our ability to conduct business.

*Further strengthened supervision of the online game industry may adversely affect our online game operation.*

In September 2009, the SAPPRFT together with the National Copyright Administration, and the National Office of Combating Pornography and Illegal Publications jointly issued a *Notice on Further Strengthening on the Administration of Pre-examination and Approval of Online Game and the Examination and Approval of Imported Online Game*, or the SAPPRFT Online Game Notice. In the SAPPRFT Online Game Notice, the SAPPRFT states that it is the only governmental department with authority for examination and pre-approval of online games, and that all online game operators must obtain an Internet publishing license to provide online game services. Under the SAPPRFT Online Game Notice, additional approvals from the SAPPRFT are required when game operators release new versions or expansion packs, or make any changes to the originally approved online game. In addition, on July 1, 2009, the SAPPRFT issued a *Notice on Strengthening the Approval and Administration of Imported Online Games*, in which the SAPPRFT stated that it is the only governmental department authorized by the State Council to approve the importation of online games from offshore copyright owners. In the event of any failure to meet the above-mentioned requirements, an operator may face heavy penalties, such as being ordered to stop operation, or having its business license revoked. Our online game business may be adversely affected by these two SAPPRFT notices. The launch of expansion packs and imported games might be delayed because of the extra approval required. Such delay in releasing expansion packs or imported games may result in higher costs for our online game operation and have an adverse effect on our game revenue.

On June 3, 2010, the MOC issued the *Interim Measures for Online Games Administration*, or the Online Game Measures, which became effective on August 1, 2010, aiming to further strengthen the MOC's supervision of the online game industry. Specifically, the Online Game Measures reiterate that the MOC has the power to review the content of all online games except online game publications that have been pre-approved by the SAPPRFT. However, the Online Game Measures do not clearly specify what constitutes "online game publication." Furthermore, the Online Game Measures provide that all domestic online games must be filed with the MOC, while all imported online games are subject to a content review prior to their launch. If a substantial change (for example, any significant modification to a game's storyline, language, tasks, or trading system) is made to an existing imported or domestic online game, it will be subject to a new content review.





Our online game business may be adversely affected by the Online Game Measures. The Online Game Measures do not set forth any specific procedure for the required filing and content review procedures for online games and therefore may cause delay when we try to file or apply for content review with the MOC. In addition, for our imported licensed games, the requirement for prior approval of any substantial change may cause delay in releasing expansion packs, which may result in higher costs of our online game operation and have an adverse effect on our game revenue. In addition, the Online Game Measures do not resolve certain inconsistencies and ambiguities resulting from pronouncements included in previous notices issued by the SAPPRFT and the MOC. Because there is ambiguity in the scope of the authority and the roles and responsibilities of governmental departments, such as the SAPPRFT and the MOC, with oversight of the online game industry, we may face stricter scrutiny of the day-to-day operations of our online game business. If any of our online game operating entities cannot comply with any of the stipulations of any PRC governmental department regarding the online game industry, we may be subject to various penalties and our online game business may be adversely affected.

*Our business may be adversely affected if we cannot obtain a payment service license*

On June 14, 2010, the PBOC issued the *Administrative Measure on the Payment Services of Non-Financial Institutions*, or the Payment Measures, which went into effect on September 1, 2010. Under the Payment Measures, Payment Services are defined as the provision of capital transfer services by non-financial institutions acting as intermediaries, including services rendered in connection with network-based payments, issuance and settlement services for pre-paid cards and acquiring services for bank cards. The Payment Measures require all non-financial institutions engaging in Payment Services to obtain a Payment Service License from the PBOC. The Payment Measures provide a one-year grace period starting September 1, 2010. Failure to obtain a Payment License will lead to the termination of the right to provide payment services. Given that the definition of “network-based payments” in the Payment Measures is vague, we are not sure whether or not our fee collection activity involved in our online game operations would constitute a kind of payment service under the Payment Measures. If we are required to apply for a Payment Service License under the Payment Measures, we cannot assure you that we will be able to obtain the required license in a timely manner. If we cannot obtain such license, our business will be adversely affected.

***Risks Related to Our Acquisition of Certain Assets of the 17173 Business from Sohu and Our Continuing Relationship with Sohu***

*Our financial information included in this annual report includes the 17173 Business, which we acquired on December 15, 2011, as if we had owned and operated it throughout each of the years presented and may not be representative of the results that the 17173 Business would have achieved had we owned and operated it prior to the date we acquired it.*

The consolidated financial statements included in this annual report were prepared as if we had owned and operated the 17173 Business, the acquisition of certain assets of which we completed on December 15, 2011, for all of the year ended December 31, 2011. Our consolidated financial statements for the year ended December 31, 2011, and our selected consolidated data presented as of December 31, 2011 and for the year then ended, as well as the years ended December 31, 2009 and 2010, may not necessarily reflect the results of operations, financial position and cash flows we would have experienced with respect to the 17173 Business if we had owned and operated it throughout those years. See “Related Party Transactions—Transactions Agreements for Our Purchase of the 17173 Business” in Item 7, “Selected Consolidated Financial Data” in Item 3 and the notes to our consolidated financial statements included elsewhere in this annual report.

*We may not be able to continue to receive the same level of support from Sohu and may not be successful in establishing our brand identity.*

Sohu has been a leading Internet portal in China, and our business has benefited significantly from Sohu’s strong Internet market position in China. For example, we have benefited from marketing and advertising across Sohu’s domains (such as Sohu.com, the Sohu portal), and using Sohu’s email system and the Sohu Group’s single-user ID system, which provide Sohu’s large number of registered users easy access to our games. Following our acquisition of the 17173 Business, Sohu will continue to provide links and advertising space on Sohu’s Websites and related technical support to us in connection with our operation of the 17173 Business. We also benefit from the strong brand recognition of Sohu in China, which has provided us a broad marketing reach.

Although we entered into a series of agreements with Sohu in connection with our acquisition of the 17173 Business, we cannot assure you we will receive adequate support from Sohu for the 17173 Business.



*Our agreements with Sohu may be less favorable to us than similar agreements negotiated between unaffiliated third parties. In particular, our Non-Competition Agreement with Sohu limits the scope of business that we are allowed to conduct.*

We entered into a Non-Competition Agreement (which was amended and restated on November 29, 2011), a Marketing Services Agreement and other related agreements with Sohu prior to our initial public offering and the terms of such agreements may be less favorable to us than would be the case if they were negotiated with unaffiliated third parties. In particular, under the Non-Competition Agreement that we entered into with Sohu, we are prohibited during the non-competition period (which commences on January 1, 2009 and ends on the later of three years after Sohu no longer owns in the aggregate at least 10% of the voting power of our then outstanding voting securities and March 17, 2014) from entering into the online portal, search, or mobile value-added services or any other business conducted or contemplated to be conducted by Sohu as of April 1, 2009, except the MMORPG business. As amended and restated on November 29, 2011, the Non-Competition Agreement does not prohibit us from engaging in the 17173 Business and prohibits Sohu from competing with the 17173 Business until December 15, 2016. Sohu currently offers Internet portal, search and mobile value-added services. Such contractual limitations significantly affect our ability to diversify our revenue source and may adversely impact our business and results of operations should the growth of MMOGs in China slow down. Moreover, so long as Sohu continues to control us, we may not be able to bring a legal claim against Sohu in the event of contractual breach, notwithstanding our contractual rights under the Non-Competition Agreement and Marketing Services Agreement described above and other inter-company agreements entered into from time to time.

*Sohu controls the outcome of shareholder actions in our company.*

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of Class A ordinary shares are entitled to one vote per share, while holders of Class B ordinary shares are entitled to 10 votes per share. We issued Class A ordinary shares represented by our ADSs in our initial public offering and Sohu holds Class B ordinary shares. As of February 21, 2014, Sohu held approximately 67.9% of the combined total of Changyou's outstanding Class A and Class B ordinary shares and controlled approximately 83.0% of the total voting power in Changyou due to the additional voting power of the Class B ordinary shares it holds. Sohu's voting power gives it the power to control actions that require shareholder approval under Cayman Islands law, our memorandum and articles of association and NASDAQ requirements, including the election and removal of any member of our board of directors, significant mergers and acquisitions and other business combinations, changes to our memorandum and articles of association, the number of shares available for issuance under share incentive plans, and the issuance of significant amounts of our ordinary shares in private placements. Due to the disparate voting powers attached to the two classes of our ordinary shares, Sohu has sufficient voting power to determine the outcome of all matters requiring shareholder approval even if it should, at some point in the future, hold considerably less than a majority of the combined total of our outstanding Class A and Class B ordinary shares.

Sohu's voting control may cause transactions to occur that might not be beneficial to the holders of ADSs, and may prevent transactions that would be beneficial to them. For example, Sohu's voting control may prevent a transaction involving a change of control of us, including transactions in which a holder of our ADSs might otherwise receive a premium for such securities over the then-current market price. In addition, Sohu is not prohibited from selling a controlling interest in us to a third party and may do so without approval of the holders of our ADSs and without providing for a purchase of outstanding ADSs. If Sohu is acquired or otherwise undergoes a change of control, or sells a controlling interest in us, any acquiror or successor will be entitled to exercise the voting control and contractual rights of Sohu, and may do so in a manner that could vary significantly from that of Sohu.

*We may have conflicts of interest with Sohu and, because of Sohu's controlling ownership interest in our company, may not be able to resolve such conflicts on favorable terms for us.*

Conflicts of interest may arise between Sohu and us in a number of areas relating to our past and ongoing relationships. Potential conflicts of interest that we have identified include the following:

- **Indemnification arrangements with Sohu.** We have agreed to indemnify Sohu with respect to lawsuits and other matters relating to our MMORPG business, including operations of that business when it was a business unit of Sohu prior to the carve-out transactions. These indemnification arrangements could result in our having interests that are adverse to those of Sohu; for example, we might have different interests with respect to settlement arrangements in a litigation matter. In addition, under these arrangements, we agreed to reimburse Sohu for liabilities incurred (including legal defense costs) in connection with litigation, while Sohu will be the party prosecuting or defending the litigation.



- **Non-competition arrangements with Sohu.** We and Sohu have each agreed not to compete with the core business of each other. Sohu has agreed not to compete with us anywhere in the world in the MMORPG business during the non-competition period (which commenced on January 1, 2009 and ends on the later of three years after Sohu no longer owns in the aggregate at least 10% of the voting power of our then outstanding voting securities and March 17, 2014) and in the 17173 Business until December 15, 2016. We have agreed not to compete with Sohu in the Internet portal, search, mobile value-added services and any other businesses conducted or contemplated to be conducted by Sohu as of the date of the prospectus for our initial public offering, except for the 17173 Business after we acquired it from Sohu on December 15, 2011. Sohu's continued operation of a Website through the domain name "games.sohu.com," however, including providing links through that Web site to MMOGs and other games, even if they are operated by our competitors, will not constitute a violation by Sohu of its agreement not to compete with us in the 17173 Business, as long as content for and maintenance of such site is primarily provided by our staff.
- **Employee recruiting and retention.** Because both Sohu and we operate primarily in Beijing and, after our acquisition of the 17173 Business, both Sohu and we are engaged in the development and operation of online portals and the operation of Web games, we may compete with Sohu in the hiring of new employees, in particular with respect to software development. We have a non-solicitation arrangement with Sohu that restricts Sohu and us from hiring any of the other's employees.
- **Our board members or executive officers may have conflicts of interest.** Dr. Charles Zhang, our Chairman of the Board, is currently also serving as Sohu's Chairman and Chief Executive Officer. Some of our board members and executive officers also own shares, restricted share units and/or options in Sohu. Sohu may grant incentive share compensation to our board members and executive officers from time to time. These relationships could create, or appear to create, conflicts of interest when these persons are faced with decisions with potentially different implications for Sohu and us.
- **Sale of shares in our company.** Sohu may decide to sell all or a portion of our shares that it holds to a third party, including to one of our competitors, thereby giving that third party substantial influence over our business and our affairs. Such a sale could be contrary to the interests of certain of our shareholders, including our employees or our public shareholders.
- **Allocation of business opportunities.** Business opportunities may arise that both we and Sohu find attractive, and which would complement our respective businesses. Sohu may decide to take the opportunities itself, which would prevent us from taking advantage of the opportunity ourselves.
- **Developing business relationships with Sohu's competitors.** So long as Sohu remains as our controlling shareholder, we may be limited in our ability to do business with its competitors, such as other Internet portals in China. This may limit the effectiveness of our online advertisement for the best interest of our company and our other shareholders.
- **Strategic decisions by Sohu, our controlling shareholder, affecting us that we might not have made.** Although our company is a separate, stand-alone entity, we expect to operate, for as long as Sohu is our controlling shareholder, as a part of the Sohu Group. Sohu may from time to time make strategic decisions that it believes are in the best interests of its business as a whole, including our company. These decisions may be different from the decisions that we would have made on our own. Sohu's decisions with respect to us or our business may be resolved in ways that favor Sohu and therefore Sohu's own shareholders, which may not coincide with the interests of our other shareholders.

We may not be able to resolve any potential conflicts, and even if we do so, the resolution may be less favorable to us than if we were dealing with an unaffiliated shareholder. Even if both parties seek to transact business on terms intended to approximate those that could have been achieved among unaffiliated parties, this may not succeed in practice.

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

*Adverse changes in political and economic policies of the PRC government could have a material and adverse effect on the overall economic growth of China, which could reduce the demand for our products.*

Most of our business operations are conducted in China and most of our revenues are generated in China. Accordingly, our business, financial condition, results of operations and prospects are affected significantly by economic, political and legal developments in China. The Chinese economy differs from the economies of most developed countries in many respects, including the amount of government involvement, the level of development, the growth rate, the control of foreign exchange, and the allocation of resources.





While the Chinese economy has grown significantly in the past 30 years, the growth has been uneven geographically among various sectors of the economy, and during different periods. The Chinese economy may not continue to grow, and if there is growth, such growth may not be steady and uniform; if there is a slowdown, such a slowdown may have a negative effect on our business. The Chinese economy experienced high inflation in 2010 and 2011, and to curb the accelerating inflation the PBOC, China's central bank, raised benchmark interest rates three times in 2011. Partly as a result of these measures, the real estate market in the PRC experienced significant declines in those years. The level of exports from the PRC also declined significantly recently. According to the National Bureau of Statistics of China, the growth rate of China's gross domestic product, compared to that of the same period in the previous year, slowed from 9.2% in 2011, 7.5% in 2012 and 7.7% in 2013. Various macroeconomic measures and monetary policies adopted by the PRC government to guide economic growth and manage inflation and the allocation of resources may not be effective in sustaining the growth rate of the Chinese economy. In addition, such measures, even if they benefit the overall Chinese economy in the long run, may have an adverse effect on us if they reduce the disposable income of our game players or if they cause our advertising clients to reduce their spending for our online advertising services on the 17173.com Website.

*Uncertainties with respect to the Chinese legal system could have a material adverse effect on us.*

We conduct most of our operations through our wholly foreign-owned subsidiaries in the PRC, AmazGame, 7Road Technology, Gamespace and ICE Information, and our variable interest entities in the PRC, Gamease, Shenzhen 7Road, Guanyou Gamespace, Doyo and Shanghai ICE. Our PRC subsidiaries are generally subject to laws and regulations applicable to foreign investment in China and, in particular, laws applicable to WFOEs. Our VIEs are generally subject to laws applicable to domestic companies in China. The PRC legal system is based on written statutes and regulations. Prior court decisions may be cited for reference but have limited precedential value. Although since 1979 PRC law has significantly enhanced the protections afforded to various forms of foreign investments in China, the PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform and enforcement of these laws, regulations and rules involves uncertainties. We cannot predict the effect of future developments in the PRC legal system, including the promulgation of new laws, changes to existing laws or the interpretation or enforcement thereof, the preemption of local regulations by national laws, or the overturn of local government's decisions by the higher level government. These uncertainties may limit legal protections available to us. In addition, any litigation in China may be protracted and result in substantial costs and diversion of resources and management attention.

*Contract drafting, interpretation and enforcement in China involve significant uncertainty.*

We have entered into numerous contracts governed by PRC law, many of which are material to our business. As compared with contracts in the United States, contracts governed by PRC law tend to contain less detail and are not as comprehensive in defining contracting parties' rights and obligations. As a result, contracts in China are more vulnerable to disputes and legal challenges. In addition, contract interpretation and enforcement in China is not as developed as in the United States, and the result of any contract dispute is subject to significant uncertainties. Therefore, we may be subject to disputes under our material contracts, and if such disputes arise, we may not prevail. Due to the materiality of certain contracts to our business, such as our license agreements with Louis Cha regarding our rights to develop and operate TLBB, any dispute involving such contracts, even without merit, may materially and adversely affect our reputation and our business operations, and may cause the price of our ADSs to decline.

*PRC law establishes complex procedures for some acquisitions of Chinese companies by foreign investors, which could make it more difficult for us to make acquisitions in China.*

Applicable PRC law and regulations, such as the Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, or the M&A Rules, which became effective on September 8, 2006 and were amended on June 22, 2009, the Anti-Monopoly Law, which became effective on August 1, 2008, the Notice on Establishing the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors promulgated by the General Office of the State Council and the MOFCOM Security Review Rules, mandate procedures and requirements, including requirements in some instances that the MOFCOM be notified in advance of any change-of-control transaction in which a foreign investor takes control of a PRC domestic enterprise, or that approval from the MOFCOM be obtained in circumstances where overseas companies established or controlled by PRC enterprises or residents acquire affiliated domestic companies, that can be expected to make merger and acquisition activities in China by foreign investors time-consuming and complex. PRC law also requires certain merger and acquisition transactions to be subject to a security review. The MOFCOM Security Review Rules, which became effective September 1, 2011, provide that, when deciding whether a specific merger or acquisition of a domestic enterprise by foreign investors is subject to a security review by the MOFCOM, the principle of substance over form should be applied, and foreign investors are prohibited from bypassing the security review requirement by structuring transactions through proxies, trusts, indirect investments, leases, loans, or control through contractual arrangements. Factors that the MOFCOM considers in its review are whether (i) an important industry is concerned, (ii) such transaction involves factors that have had or may have an impact on national economic security and (iii) such transaction will lead to a change in control of a domestic enterprise that holds a well-known PRC trademark or a time-honored PRC brand. If the business of any target company that we plan to acquire falls into the ambit of security review, we may not be able to successfully acquire such company. Complying with the requirements of the relevant regulations to complete such transactions could be time-consuming, and any required approval process, including approval from the MOFCOM, may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business.



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*There are significant uncertainties under the Corporate Income Tax Law of the PRC, or the CIT Law, regarding our PRC enterprise income tax liabilities, such as tax on dividends paid to us by our PRC subsidiaries. The CIT Law also contains uncertainties regarding possible PRC withholding tax on any dividends we pay to our overseas corporate shareholders and gains realized from the transfer of our shares by our overseas corporate shareholders.*

We are a holding company incorporated in the Cayman Islands which indirectly holds, through our Hong Kong subsidiaries, our equity interests in our subsidiaries in the PRC. Our business operations are principally conducted by these PRC subsidiaries and our VIEs. The CIT Law and its implementation rules provide that China-sourced income of foreign enterprises, such as dividends paid by a PRC subsidiary to its overseas parent, will normally be subject to PRC withholding tax at a rate of 10%, unless there are applicable tax treaties that reduce such rate. Under the *Arrangement Between the PRC and the Hong Kong Special Administrative Region on the Avoidance of Double Taxation and Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital*, or the China-HK Tax Arrangement, the dividend withholding tax rate may be reduced to 5%, if a Hong Kong resident enterprise is considered a non-PRC tax resident enterprise and holds at least 25% of the equity interests in the PRC enterprise distributing the dividends, subject to approval of the PRC local tax authority. However, if the Hong Kong resident enterprise is not considered to be the beneficial owner of such dividends under applicable PRC tax regulations, such dividends may remain subject to withholding tax at a rate of 10%. On October 27, 2009, the SAT, issued a *Notice on How to Understand and Determine the Beneficial Owners in Tax Agreement*, or Circular 601, which provides guidance on determining whether an enterprise is a “beneficial owner” under China’s tax treaties and tax arrangements. Circular 601 provides that, in order to be a beneficial owner, an entity generally must be engaged in substantive business activities, and that a company that is set up for the purpose of avoiding or reducing taxes or transferring or accumulating profits, will not be regarded as a beneficial owner and will not qualify for treaty benefits such as preferential dividend withholding tax rates. We are in the process of applying for qualification as a “beneficial owner” for each of our Hong Kong subsidiaries with the SAT. If any of our Hong Kong subsidiaries is, in the light of Circular 601, determined by the SAT to be a non-beneficial owner for purposes of the China-HK Tax Arrangement, any dividends paid to it by any of our PRC subsidiaries would not qualify for the preferential dividend withholding tax rate of 5%, but rather would be subject to the usual CIT Law rate of 10%.

We believe we are not a PRC tax resident enterprise, but it is not clear whether we or any of our Hong Kong subsidiaries will be deemed to be PRC tax residents under the CIT Law. The tax resident status of an enterprise is subject to determination by the PRC tax authorities and uncertainties remain with respect to the interpretation of the term “de facto management body.” Under the CIT Law and its implementation rules, an enterprise established outside of the PRC with a “de facto management body” within the PRC is considered a resident enterprise and will be subject to the enterprise income tax on its global income at the rate of 25%. The implementation rules define the term “de facto management body” as the body that exercises full and substantial control and overall management over the business, productions, personnel, accounts and properties of an enterprise. On April 22, 2009, the SAT issued a circular, known as Circular 82, which provides certain specific criteria for determining whether the “de facto management body” of a PRC-controlled enterprise that is incorporated offshore is located in China. Although this circular only applies to offshore enterprises controlled by PRC enterprises or PRC enterprise groups, not those controlled by PRC individuals or foreigners, the criteria set forth in the circular may reflect the SAT’s general position on how the “de facto management body” text should be applied in determining the tax resident status of all offshore enterprises. Under Circular 82, an offshore incorporated enterprise controlled by a PRC enterprise or a PRC enterprise group will be regarded as a PRC tax resident by virtue of having its “de facto management body” in China and will be subject to PRC enterprise income tax on its global income only if all of the following conditions are met: (i) the primary location of the day-to-day operational management is in the PRC; (ii) decisions relating to the enterprise’s financial and human resource matters are made or are subject to approval by organizations or personnel in the PRC; (iii) the enterprise’s primary assets, accounting books and records, company seals, and board and shareholder resolutions, are located or maintained in the PRC; and (iv) at least 50% of voting board members or senior executives habitually reside in the PRC. If we are considered as a PRC tax resident under the CIT law by the PRC tax authorities, our global income will be subject to corporate income tax at a rate of 25%.

Although we intend to take the position that any dividends we pay to our overseas corporate shareholders or ADS holders will not be subject to a withholding tax in the PRC, if we or any of our Hong Kong subsidiaries are considered to be PRC tax resident enterprises for tax purposes, any dividends we pay to our overseas corporate shareholders or ADS holders as well as gains realized by such shareholders or ADS holders from the transfer of our shares or ADSs may be regarded as China-sourced income and as a result be subject to PRC withholding tax at a rate up to 10%. The implementation rules of the CIT Law provide that, if an enterprise that distributes dividends is domiciled in the PRC or if gains are realized from transferring equity interests of an enterprise domiciled in the PRC, then such dividends or gains are treated as “China-sourced income.” However, it is not clear how “domicile” might be interpreted under the CIT Law, and it is possible that domicile could be interpreted to mean the jurisdiction where the enterprise is a tax resident.



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Due to the lack of interpretation of the CIT Law, it is difficult to ascertain how it will be implemented by the relevant PRC tax authorities. If dividend payments from Changyou HK, ICE HK or other overseas subsidiaries to us are subject to PRC withholding tax, our financial condition, results of operations and the amount of dividends available to pay our shareholders may be adversely affected. If dividends we pay to our overseas shareholders or ADS holders or gains realized by such shareholders or ADS holders from the transfer of our shares or ADSs are subject to PRC withholding tax, the withholding tax will generally be at a rate of 10% and reduce their investment return and the value of their investments in us.

*Heightened scrutiny of acquisition transactions by PRC tax authorities may have a negative impact on our business operations, our acquisition strategy or the value of your investment in us.*

Pursuant to the *Notice on Strengthening Administration of Enterprise Income Tax for Share Transfers by Non-PRC Resident Enterprises*, or SAT Circular 698, issued by the SAT with effect from January 1, 2008, where a non-resident enterprise transfers the equity interests of a PRC tax resident enterprise indirectly by disposition of the equity interests of an overseas holding company, or an Indirect Transfer, and such overseas holding company is located in a tax jurisdiction that has an effective tax rate of less than 12.5% and does not impose income tax on foreign income of its residents, the non-resident enterprise must report the Indirect Transfer to tax authorities in the PRC. Using a “substance over form” principle, the PRC tax authorities may disregard the existence of the overseas holding company if it lacks a reasonable commercial purpose and was established for the purpose of reducing, avoiding or deferring PRC tax. As a result, gains derived from an Indirect Transfer may be subject to PRC withholding tax at a rate of up to 10%. SAT Circular 698 also provides that, where a non-PRC resident enterprise transfers its equity interests in a PRC tax resident enterprise to related parties of the non-PRC resident enterprise at a price lower than the fair market value, the PRC tax authorities have the power to make a reasonable adjustment to the taxable income resulting from the transaction.

The SAT released the *Announcement on Several Issues concerning the Administration of Income Tax of Non-tax-resident Enterprises*, or SAT Public Notice 24, which became effective on April 1, 2011, to clarify several issues related to Circular 698. Under SAT Public Notice 24, the term “effective tax” refers to the effective tax on the gain derived from the disposition of equity interests of an overseas holding company; and the term “does not impose income tax” refers to cases where the gain derived from disposition of the equity interests of an overseas holding company is not subject to income tax in the country or region where the overseas holding company is a resident.

There is uncertainty as to the application of SAT Circular 698. For example, while the term “Indirect Transfer” is not clearly defined, it appears that PRC tax authorities are authorized to request information from a wide range of foreign entities that have no direct link to China. Moreover, the relevant PRC authorities have not issued any formal rules as to the process and format for reporting an Indirect Transfer to the PRC tax authorities. In addition, there are not any formal rules as to how it is determined whether a foreign investor lacks a commercial purpose and was established in order to reduce, avoid or defer PRC tax. SAT Circular 698 may be determined by PRC tax authorities to be applicable to the historical reorganization of 7Road, including our acquisition of the equity interests of 7Road, if any of the steps in 7Road’s reorganization were determined by PRC tax authorities to lack a reasonable commercial purpose. As a result, the transfer of 7Road’s shares by certain shareholders to other parties may be subject to income tax on capital gains generated from such transfers of the shares, and PRC tax authorities might, at their discretion, adjust any capital gains and impose tax return filing obligations on the transferring shareholders or require us to provide assistance for an investigation by PRC tax authorities. Furthermore, although SAT Circular 698 contains an exemption for transfers of publicly traded stock in a PRC tax resident enterprise, it remains unclear whether we will be deemed a PRC tax resident enterprise and whether such exemption will be applicable to the transfer of our shares or ADSs. If we are regarded as a non-PRC tax resident enterprise, PRC tax authorities may deem any future transfer of our ordinary shares or ADSs by our shareholders or holders of our ADSs to be subject to these regulations, which may subject such shareholders or holders of our ADSs to additional reporting obligations or tax burdens. In the case of failure to comply with these circulars by such shareholders or holders of our ADSs, the PRC tax authorities may take actions, including requesting us to provide assistance for their investigation, which could have a negative impact on our business operations. In addition, since we may pursue acquisitions as one of our growth strategies, and may conduct acquisitions involving complex corporate structures, PRC tax authorities might, at their discretion, adjust the amount of capital gains or request that we submit additional documentation for their review in connection with any potential acquisitions, which may cause us to incur additional acquisition costs or delay our acquisition timetable.

*As the special tax statuses of certain of our PRC subsidiaries or VIEs as “High and New Technology Enterprises” (or NHTEs), “software enterprises” or “Key National Software Enterprises” (or KNSE Companies) expire, or if they are revoked, we will have to pay additional taxes to make up any previously unpaid tax and will be subject to a higher tax rate.*

The CIT Law applies a uniform statutory income tax rate of 25% to enterprises in China. Under the CIT Law, NHTEs enjoy a favorable tax rate of 15%. The implementation rules promulgated under the CIT Law also emphasize that the ownership of “core proprietary intellectual property” is essential to qualification for this preferential tax rate. AmazGame and Gamease were subject to a 15% income tax rate as NHTEs for the years ended December 31, 2012 and 2013. The NHTE status of both AmazGame and Gamease will expire on September 15, 2014 if it is not renewed. In addition, AmazGame is qualified as a KNSE Company and will enjoy a further reduced preferential tax rate of 10% for 2013 and 2014.



The CIT Law and the implementation rules promulgated under the CIT Law provide that software enterprises enjoy an income tax exemption for two years beginning with their first profitable year and a 50% tax reduction to an income tax rate of 12.5% for the subsequent three years. AmazGame and Gamease qualified as software enterprises and enjoyed a 50% tax reduction to a rate of 12.5% for the year ended December 31, 2011. 7Road Technology qualified as a software enterprise in 2012 and enjoyed an income tax exemption for the 2013 fiscal year. Shenzhen 7Road qualified as a software enterprise and enjoyed a 50% tax reduction to a rate of 12.5% for the 2011, 2012 and 2013 fiscal years. Shanghai ICE qualified as a software enterprise in 2008 and enjoyed an income tax exemption for the 2011 fiscal year and enjoyed, and will enjoy, a 50% tax reduction to a rate of 12.5% for the subsequent three years. Gamespace qualified as a software enterprise and enjoyed an income tax exemption for the 2012 and 2013 fiscal years and will be entitled to a 50% tax reduction to a rate of 12.5% for the subsequent three years. ICE Information has been qualified as a software enterprise and will be entitled to an income tax exemption for two years beginning with their first profitable year and a 50% tax reduction for the subsequent three years, if they continue to maintain their qualification.

There are uncertainties regarding the future interpretation and implementation of the CIT Law. It is possible that the qualification of AmazGame and Gamease as NHTEs, or the qualification of 7Road Technology, Shenzhen 7Road, Gamespace, ICE Information and Shanghai ICE as software enterprises, or the qualification of AmazGame as a KNSE Company, or their entitlement to an income tax exemption or refund of their VAT, will be challenged in the future by their supervising authorities and be repealed, or that there may be future implementation rules that are inconsistent with current interpretations of the CIT Law. On April 1, 2013, four PRC government authorities, including the MIIT and the SAT, jointly issued the *Measures for the Administration of Software Enterprises*. Under such measures, software enterprises accredited after January 1, 2011 will be subject to a new annual review system and failing to pass the annual review may result in the revocation of an entity's status as a software enterprise. We cannot assure you that the qualification of any of our PRC subsidiaries or VIEs as a software enterprise will not be challenged in the future or whether such companies will be able to take any further actions, such as re-application for software enterprise qualification, to enjoy such preferential tax treatment. If the tax benefits AmazGame, Gamease, 7Road Technology, Shenzhen 7Road, Gamespace, ICE Information, and Shanghai ICE enjoy as NHTEs, KNSE Companies or Software Enterprises are revoked, and we are otherwise unable to qualify these companies for other income tax and VAT exemptions or reductions, our effective income tax rate or VAT rate, as the case may be, will increase significantly, which will reduce our net income. In addition, we may have to pay additional taxes to make up any previously unpaid tax, which could further reduce our net income.

*To fund any cash requirements we may have, we may need to rely on dividends, loans or advances made by our PRC subsidiaries AmazGame, 7Road Technology, Gamespace and ICE Information, which are subject to limitations and possible taxation under applicable PRC law.*

We may rely on dividends and other distributions on equity, or loans and advances made by our PRC subsidiaries AmazGame, 7Road Technology, Gamespace and ICE Information, to fund any cash requirements we may have, including the funds necessary to pay dividends and other cash distributions, if any, to our shareholders or ADS holders, and to service any debt we may incur. The distribution of dividends and the making of loans and advances by entities organized in China are subject to limitations. Regulations in the PRC currently permit payment of dividends only out of accumulated profits as determined in accordance with accounting standards and regulations in China. Each of AmazGame, 7Road Technology, Gamespace and ICE Information is also required to set aside at least 10% of its after-tax profit based on PRC accounting standards each year to its general reserves until the cumulative amount of such reserves reaches 50% of its registered capital. These reserves are not distributable as cash dividends, loans or advances. AmazGame, 7Road Technology, Gamespace and ICE Information may also allocate a portion of their after-tax profits, as determined by their boards of directors, to their staff welfare and bonus funds, which may not be distributed to us. In addition, if any of AmazGame, 7Road Technology, Gamespace and ICE Information incurs debt on its own behalf in the future, the instruments governing the debt may restrict its ability to pay dividends or make other distributions to us.

Furthermore, under regulations of the State Administration of Foreign Exchange, or the SAFE, the RMB is not convertible into foreign currencies for capital account items, such as loans, repatriation of investments and investments outside of China, unless prior approval of the SAFE is obtained and prior registration with the SAFE is made, which could delay or prevent any transfers of funds from our PRC subsidiary to us.

In addition, there are uncertainties under the CIT Law with regard to the PRC withholding tax on dividends paid by AmazGame, 7Road Technology, Gamespace and ICE Information to Changyou HK, 7Road HK or ICE HK. See "Risk Factors—Risks related to Doing Business in China—There are significant uncertainties under the Corporate Income Tax Law of the PRC, or the CIT Law, regarding our PRC enterprise income tax liabilities, such as tax on dividends paid to us by our PRC subsidiaries. The CIT Law also contains uncertainties regarding possible PRC withholding tax on any dividends we pay to our overseas corporate shareholders and gains realized from the transfer of our shares by our overseas corporate shareholders." Should such dividends be subject to PRC withholding tax or be subject to the usual CIT Law withholding tax rate of 10% rather than the preferential dividend withholding tax rate of 5% provided under the China-HK Tax Arrangement, the amount of cash available to us for our cash needs, including for the payment of dividends to our shareholders or ADS holders, would be reduced.





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Furthermore, we control our PRC operating entities Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE through contractual arrangements rather than equity ownership. AmazGame entered into a Technology Development and Support Agreement and an Operation and Maintenance Agreement with Gamease, pursuant to which Gamease will pay AmazGame for the services AmazGame provides to Gamease. 7Road Technology entered into a Technology Development and Utilization Agreement and a Service and Maintenance Agreement with Shenzhen 7Road, pursuant to which Shenzhen 7Road will pay 7Road Technology for the services 7Road Technology provides to Shenzhen 7Road. Gamespace entered into a Technology Development and Support Agreement and an Operation and Maintenance Agreement with Guanyou Gamespace, pursuant to which Guanyou Gamespace will pay Gamespace for the services Gamespace provides to Guanyou Gamespace. ICE Information entered into an Exclusive Business Cooperation Agreement, an Exclusive Technology Consulting and Service Agreement and a Business Operation Agreement with Shanghai ICE, pursuant to which Shanghai ICE will pay ICE Information for the services ICE Information provides to Shanghai ICE. See “Related Party Transactions” in Item 7. To the extent that there is any distributable profit in Gamease, Shenzhen 7Road, Guanyou Gamespace or Shanghai ICE, it may be difficult for Gamease, Shenzhen 7Road, Guanyou Gamespace or Shanghai ICE to distribute such profit to AmazGame, 7Road Technology, Gamespace or ICE Information, which may further limit the amount that AmazGame, 7Road Technology, Gamespace or ICE Information can distribute to us.

*Fluctuation in the value of the RMB may have an adverse effect on our shareholders’ investment.*

Change in the value of the RMB against the U.S. dollar, Euro and other currencies is affected by, among other things, changes in China’s political and economic conditions. 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 changed policy, the RMB is permitted to fluctuate within a narrow and managed band against a basket of certain foreign currencies. This change in policy has resulted in an approximately 35% appreciation of the RMB against the U.S. dollar between July 21, 2005 and December 31, 2013. In 2008, China’s exchange regime was further changed to a managed floating exchange rate regime based on market supply and demand. While the international reaction to the RMB revaluation has generally been positive, there remains significant international pressure on the PRC government to adopt an even more flexible currency policy, which could result in a further and more significant appreciation of the RMB against the U.S. dollar. In 2010, the PBOC announced that it had decided to proceed further with the reform of the RMB exchange rate regime to enhance the flexibility of the RMB exchange rate and that emphasis would be placed on reflecting market supply and demand with reference to a basket of currencies. While so indicating its intention to make the RMB’s exchange rate more flexible, the PBOC ruled out any sharp fluctuations in the currency or a one-off adjustment. On April 16, 2012, the PBOC enlarged the floating band of RMB’s trading prices against the U.S. dollar in the inter-bank spot foreign exchange market from 0.5% to 1% around the middle rate released by the China Foreign Exchange Trade System each day. As most of our costs and expenses are denominated in RMB, the revisions in exchange rate policy commenced in July 2005 have increased, and potential future revisions could further increase, our costs and expenses in U.S. dollar terms. In addition, our proceeds from overseas financings and from overseas game operations will decrease in value if we choose not to or are unable to convert the proceeds into RMB and the RMB appreciates against the U.S. dollar, which may reduce the value of a shareholder’s investment in our ADSs.

*Regulations relating to offshore investment activities by PRC residents may limit our ability to acquire PRC companies and could adversely affect our business.*

In October 2005, SAFE promulgated *Relevant Issues Concerning Foreign Exchange Control on Domestic Residents’ Corporate Financing and Roundtrip Investment through Offshore Special Purpose Vehicles*, or Circular 75. SAFE has further issued a series of implementation guidance. These regulations require PRC residents to register with the local SAFE branch before directly establishing or indirectly controlling any offshore company for the purpose of overseas capital financing with assets of or equity interests in PRC companies held by them. PRC residents must also file amendments to their registrations if their offshore companies experience material events involving capital variation, such as changes in share capital, share transfers, mergers and acquisitions, spin-off transactions, long-term equity or debt investments or providing guarantees. Under these regulations, PRC residents’ failure to comply with specified registration procedures may result in restrictions being imposed on the foreign exchange activities of the relevant PRC entity, including the payment of dividends and other distributions to its offshore parent, as well as restrictions on capital inflows from the offshore entity to the PRC entity.

Although we request that all of our shareholders who are PRC residents comply with Circular 75 and related rules, it is unclear how these regulations will be interpreted and implemented. In addition, it may be difficult for our ultimate shareholders or beneficial owners who are PRC residents to provide sufficient supporting documents required by the SAFE or to complete the required registration with the SAFE in a timely manner, or at all. Any failure by any of our shareholders who is a PRC resident, or is controlled by a PRC resident, to comply with relevant requirements under these regulations could subject us to fines or sanctions imposed by the PRC government, including restrictions on the ability of AmazGame, 7Road Technology, Gamespace and ICE Information to pay dividends or make distributions to us and on our ability to increase our investment in AmazGame, 7Road Technology, Gamespace and ICE Information.



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*SAFE rules and regulations may limit our ability to transfer funds we hold overseas to our subsidiaries and VIEs in the PRC, which may adversely affect our business expansion, and we may not be able to convert the net proceeds from our initial public offering into RMB to invest in or acquire any other PRC companies, or establish other VIEs in the PRC.*

On August 29, 2008, SAFE promulgated Circular 142, a notice regulating the conversion by a foreign-invested company of foreign currency into RMB by restricting how the converted RMB may be used. The notice requires that the registered capital of a foreign-invested company settled in RMB converted from foreign currencies may only be used for purposes within the business scope approved by the applicable governmental authority and 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 settled in RMB converted from foreign currencies. The use of such RMB 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 for purposes within the approved business scope. Furthermore, in November 2010 the SAFE promulgated the *Circular on the Relevant Issues of Strengthening Foreign Exchange Administration*, or Circular 59, which tightens the regulation of the use of net proceeds from overseas offerings and requires that the use of such net proceeds be consistent with the description in the prospectus for the offering. In addition, to strengthen Circular 142, on November 16, 2011 the SAFE promulgated the *Circular on Further Clarifying and Regulating Relevant Issues Concerning the Administration of Foreign Exchange under Capital Account*, or Circular 45, which prohibits a foreign invested company from converting its registered capital in foreign exchange currency into RMB for the purpose of making domestic equity investments, granting entrusted loans, repaying inter-company loans, and repaying bank loans that have been transferred to a third party. Violations of Circular 142 or related regulations can result in severe penalties, such as heavy fines. Circular 142 and related regulations may significantly limit our ability to transfer funds we hold overseas to our VIEs in the PRC through our subsidiaries in the PRC, which may adversely affect our business expansion, and we may not be able to convert such funds into RMB to invest in or acquire any other PRC companies, or establish other VIEs in the PRC.

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

Under the *Administration Measures on Individual Foreign Exchange Control* issued by the PBOC and related implementation rules issued by the SAFE, all foreign exchange transactions involving an employee share incentive plan, share option plan or similar plan participated in by PRC citizens may be conducted only with the approval of the SAFE. Under the *Notice of Issues Related to the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Listed Company*, or the *Offshore Share Incentives Rules*, issued by the SAFE on February 15, 2012, PRC citizens who are granted share options, restricted share units or restricted shares by an overseas publicly listed company are required to register with the SAFE or its authorized branch and to comply with a series of other requirements. The *Offshore Share Incentives Rule* also provides procedures for registration of incentive plans, the opening and use of special accounts for the purpose of participation in incentive plans, and the remittance of funds for exercising share options and gains realized from such exercises and sales of such options or the underlying shares, both outside and inside the PRC. We, and any of our PRC employees or members of our board of directors who have been granted share options, restricted share units or restricted shares, are subject to the *Administration Measures on Individual Foreign Exchange Control*, the related implementation rules issued by the SAFE, and the *Offshore Share Incentives Rule*. If we, or any of our PRC employees or members of our board of directors who receive or hold share options, restricted share units or restricted shares, fail to comply with these registration and other procedural requirements, we may be subject to fines and other legal or administrative sanctions.

*The enforcement of the PRC Labor Contract Law and other labor-related regulations in the PRC may adversely affect our business.*

The Standing Committee of the National People's Congress of the PRC enacted the *Labor Contract Law*, or the Labor Contract Law. The Labor Contract Law introduced specific provisions related to fixed-term employment contracts, part-time employment, probationary periods, consultation with labor unions and employee assemblies, employment without a written contract, dismissal of employees, severance, and collective bargaining to enhance previous PRC labor law. Under the Labor Contract Law, an employer is obligated to sign an unlimited-term labor contract with any employee who has worked for the employer for ten consecutive years. Further, if an employee requests or agrees to renew a fixed-term labor contract that has already been entered into twice consecutively, the resulting contract, with certain exceptions, must have an unlimited term, subject to certain exceptions. With certain exceptions, an employer must pay severance to an employee where a labor contract is terminated or expires. In addition, the PRC governmental authorities have continued to introduce various new labor-related regulations since the effectiveness of the Labor Contract Law in 2008. For example, there are regulations which require that annual leave ranging from five to 15 days be made available to employees and that employees be compensated for any unused annual leave days at a rate of three times their daily salary, subject to certain exceptions.

Under the *PRC Social Insurance Law* and the *Administrative Measures on Housing Fund*, employees are required to participate in pension insurance, work-related injury insurance, medical insurance, unemployment insurance, maternity insurance and housing funds and employers are required, together with their employees or separately, to pay the social insurance premiums and housing funds for their employees.



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These laws designed to enhance labor protection tend to increase our labor costs. In addition, as the interpretation and implementation of these regulations are still evolving, our employment practices may not be at all times be deemed in compliance with the regulations. As a result, we could be subject to penalties or incur significant liabilities in connection with labor disputes or investigations.

### ***Risks Related to Our Class A Ordinary Shares and ADSs***

*We are a Cayman Islands company and, because judicial precedent regarding the rights of shareholders is more limited under Cayman Islands law than that under U.S. law, our shareholders may have less protection for their shareholder rights than they would under U.S. law.*

Our corporate affairs are governed by our memorandum and articles of association, the Companies Law, Cap 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands and the common law of the Cayman Islands. The rights of shareholders to take action against our directors, actions by minority shareholders and the fiduciary responsibilities of our directors to us under Cayman Islands law are to a large extent governed by the common law of the Cayman Islands. The common law of the Cayman Islands is derived in part from comparatively limited judicial precedent in the Cayman Islands as well as from English common law, which has persuasive, but not binding, authority on a court in the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors under Cayman Islands law are not as clearly established as they would be under statutes or judicial precedent in some jurisdictions in the United States. In particular, the Cayman Islands has a less developed body of securities laws than the United States.

*Holders of our ADSs may have difficulty enforcing judgments obtained against us.*

We are a Cayman Islands company and all of our assets are located outside the United States. A substantial portion of our current operations are conducted in the PRC. In addition, all of our directors and executive officers are nationals and residents of countries other than the United States. A substantial portion of the assets of these persons are located outside the United States. As a result, it may be difficult for holders of our ADSs to effect service of process within the United States upon these persons. It may also be difficult for holders of our ADSs to enforce in Cayman Islands courts or PRC courts judgments obtained in U.S. courts based on the civil liability provisions of the U.S. federal securities laws against us and our officers and directors, most of whom are not residents in the United States and the substantial majority of whose assets are located outside of the United States. In addition, there is uncertainty as to whether the courts of the Cayman Islands or the PRC would recognize or enforce judgments.

*Our operating results for a particular period could fall below our expectations or the expectations of investors or research analysts, resulting in a decrease in the price of our ADSs.*

Our operating results may vary significantly from period to period as a result of factors beyond our control, such as the slowdown in China's economic growth that occurred between the first quarter of 2010 and third quarter of 2012, caused in part by measures adopted by the Chinese government intended to slow such growth and to temper real estate prices and inflation, and the significant instability recently experienced in the worldwide economy, with growth in the United States slowing, and the European Community facing disruptions as a result of crises in the economies of Greece and Spain, among other countries, and such factors may be difficult to predict for any given period. Other factors also could cause significant fluctuations in our operating results, including the timing and success of our new game launches, our costs of developing and launching new games and software, and the level of user activity of our games and software in China during particular fiscal quarters. If our operating results for any period fall below our expectations or the expectations of investors or research analysts, the price of our ADSs is likely to decrease.





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*Recent press reports concerning possible increased scrutiny by Chinese authorities of the VIE structure used by us and various other Chinese companies publicly-traded in the United States appear to have created concern among investors and caused the price of the ADSs of various Chinese companies that are publicly traded in the United States to drop, and the matters highlighted in such reports may have such an effect on the price of our ADSs following this offering.*

Various prominent western news outlets have reported that the MOFCOM and the CSRC, among other Chinese regulatory authorities, may be considering increased scrutiny or enhanced regulation of Chinese companies that use VIE structures, such as we do, as a means of complying with Chinese laws restricting foreign ownership of certain businesses in China, including online game businesses such as ours. Some of such news reports have also sought to draw a connection between widely reported accounting issues at certain Chinese companies and the use of VIE structures. Such news reports appear to have had the effect of causing significant drops in the market prices of the shares of many Chinese companies. It is possible that in the future there will be increased scrutiny or enhanced regulation by Chinese regulatory authorities of Chinese companies, including us, that use the VIE structure. In addition, while we are not aware of any causal connection between the recently reported accounting scandals and the use of VIE structures, it is possible that holders or potential purchasers of our ADSs will believe that such a connection exists. Any of such circumstances could lead to further loss of investor confidence in Chinese companies and cause fluctuations in the market prices of our ADSs and, if such prices were to drop sharply, could subject us to shareholder litigation, which could cause the price for our shares to drop further.

*Registered public accounting firms in China, including our independent registered public accounting firm, are not inspected by the U.S. Public Company Accounting Oversight Board, which deprives us and our investors of the benefits of such inspection.*

Auditors of companies whose shares are registered with the U.S. Securities and Exchange Commission, or the SEC, and traded publicly in the United States, including our independent registered public accounting firm, must be registered with the U.S. Public Company Accounting Oversight Board, or the PCAOB, and are required by the laws of the United States to undergo regular inspections by the PCAOB to assess their compliance with the laws of the United States and professional standards applicable to auditors. Our independent registered public accounting firm is located in, and organized under the laws of, the PRC, which is a jurisdiction where the PCAOB, notwithstanding the requirements of U.S. law, is currently not able to freely conduct inspections without the approval of the Chinese authorities, which approval has to date been given only on a limited basis.

This lack of PCAOB inspections in China prevents the PCAOB from fully evaluating audits and quality control procedures of our independent registered public accounting firm. As a result, we and investors in our ADSs are deprived of the benefits of such PCAOB inspections. The inability of the PCAOB to conduct inspections of auditors in China makes it more difficult to evaluate the effectiveness of our independent registered public accounting firm's audit procedures or quality control procedures as compared to auditors outside of China that are subject to PCAOB inspections, which could cause investors and potential investors in our ADSs to lose confidence in our audit procedures and reported financial information and the quality of our financial statements, and result in a drop in the market price of our ADSs.

*If a recent initial decision rendered by the Administrative Law Judge (the "ALJ") in administrative proceedings brought by the SEC against the Big Four PRC-based accounting firms, including our independent registered public accounting firm, becomes final, we could be unable to timely file future financial statements in compliance with the requirements of the Securities Exchange Act of 1934.*

In December 2012, the SEC instituted administrative proceedings against the Big Four PRC-based accounting firms, including our independent registered public accounting firm, alleging that these firms had violated U.S. securities laws and the SEC's rules and regulations thereunder by failing to provide to the SEC the firms' audit work papers with respect to certain PRC-based companies that are publicly traded in the United States. On January 22, 2014, the ALJ presiding over the matter rendered an initial decision that each of the firms had violated the SEC's rules of practice by failing to produce audit workpapers to the SEC. The initial decision censured each of the firms and barred them from practicing before the SEC for a period of six months. The Big Four PRC-based accounting firms recently appealed the ALJ's initial decision to the SEC. The ALJ's decision does not take effect unless and until it is endorsed by the SEC. Any SEC endorsement or other determination could be appealed by the accounting firms through the U.S. federal courts. While we cannot predict the outcome of the SEC's review or that of any subsequent appeal process, if the accounting firms are ultimately temporarily denied the ability to practice before the SEC, our ability to file our financial statements in compliance with SEC requirements could be impacted. A determination that we have not timely filed financial statements in compliance with SEC requirements could ultimately lead to the delisting of our ADSs from NASDAQ or the termination of the registration of our ADSs and Class A ordinary shares under the Securities Exchange Act of 1934, or both, which would substantially reduce or effectively terminate the trading of our ADSs in the United States.



*We are a “controlled company” within the meaning of the NASDAQ Listing Rules and, as a result, we rely on exemptions from certain corporate governance requirements that provide protection to shareholders of other companies, and if in the future we are no longer a “controlled company,” we may invoke the “home country” exceptions under the NASDAQ Listing Rules which provide for similar exemptions for foreign private issuers such as us.*

Because Sohu owns more than 50% of the total voting power of our ordinary shares, we are a “controlled company” under the NASDAQ Listing Rules. We rely on certain exemptions that are available to controlled companies from NASDAQ corporate governance requirements, including the requirements:

- that we have a corporate governance and nominating committee that is composed entirely of independent directors with a written charter addressing the committee’s purpose and responsibilities;
- that we have a compensation committee that is composed entirely of independent directors with a written charter addressing the committee’s purpose and responsibilities; and
- for an annual performance evaluation of the nominating and governance committee and compensation committee.

We are not required to and will not voluntarily meet these requirements. If we are no longer a “controlled company,” we may in the future invoke the “home country” exceptions available to foreign private issuers, such as us, under the NASDAQ Listing Rules which are similar to the exemptions for controlled companies. As a result of our use of the “controlled company” exemptions, and any future use by us of the “home country” exceptions, holders of our ADSs will not have the same protection afforded to shareholders of companies that are subject to all of NASDAQ’s corporate governance requirements.

*The market price for our ADSs has been and may continue to be volatile.*

The trading price of our ADSs has been and may continue to be subject to wide fluctuations. During the period from April 2, 2009, the first day of trading of our ADSs on the NASDAQ Global Select Market, until February 21, 2014, the trading price of our ADSs ranged from \$17.00 to \$52.00 per ADS, and the closing sale price on February 21, 2014 was \$28.87 per ADS. The market price for our ADSs may continue to be volatile and subject to wide fluctuations in response to factors including the following:

- announcements of competitive developments, including new games by our competitors;
- regulatory developments in our target markets affecting us, our customers or our competitors;
- actual or anticipated fluctuations in our quarterly operating results;
- failure of our quarterly financial and operating results to meet market expectations or failure to meet our previously announced guidance;
- changes in financial estimates by securities research analysts;
- changes in the economic performance or market valuations of other Internet or online game companies;
- additions or departures of our executive officers and other key personnel;
- announcements regarding intellectual property litigation (or potential litigation) involving us or any of our directors and officers;
- fluctuations in the exchange rates between the U.S. dollar and the RMB;
- release or expiration of transfer restrictions on our outstanding ordinary shares and ADSs; and
- sales or perceived sales of additional shares or ADSs.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are not related to the operating performance of particular industries or companies. Such market fluctuations may have a material adverse effect on the market price of our ADSs.

*Holders of our ADSs may be subject to limitations on transfer of their ADSs.*

Our ADSs are transferable on the books of the depository. However, the depository may close its transfer books at any time or from time to time when it deems it expedient in connection with the performance of its duties. In addition, the depository may refuse to deliver, transfer or register transfers of ADSs generally when our books or the books of the depository are closed, or at any time if we or the depository deem it advisable to do so because of any requirement of law or of any government or governmental body, or under any provision of the Deposit Agreement, or for any other reason.



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*Holders of ADSs have limited voting rights and may not receive voting materials in time to be able to exercise their right to vote.*

Except as described in this annual report and in the Deposit Agreement, holders of our ADSs will not be able to exercise voting rights attaching to the shares represented by our ADSs on an individual basis. Holders of our ADSs may instruct the depositary how to exercise the voting rights attaching to the shares represented by the ADSs. Holders may not receive voting materials in time to instruct the depositary to vote, and it is possible that direct holders of ADSs, or persons who hold their ADSs through brokers, dealers or other third parties, will not have the opportunity to exercise a right to vote. In addition, due to the different voting powers attached to the two classes of our ordinary shares, our controlling shareholder, Sohu, our Chief Executive Officer, or CEO, Tao Wang, and certain of our directors, officers and key employees, all of which hold our Class B ordinary shares, control 97% of the combined total voting power of our ordinary shares. As a result, the ability of holders of our ADSs to affect the outcome of any matter subject to shareholder vote is very limited.

*ADS holders' right to participate in any future rights offerings may be limited, which may cause dilution to their holdings and ADS holders may not receive cash dividends if it is impractical to make them available to such holders.*

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. However, we cannot make rights available to ADS holders in the United States unless we register the securities to which the rights relate under the Securities Act of 1933, or the Securities Act, or an exemption from registration requirements is available. Also, under the Deposit Agreement, the depositary bank will not make rights available to ADS holders unless the distribution to ADS holders of both the rights and any related securities are either registered under the Securities Act or exempted from registration under the Securities Act. We are under no obligation to file a registration statement with respect to any such rights or securities or to endeavor to cause such a registration statement to be declared effective. Moreover, we may not be able to establish an exemption from registration under the Securities Act. Accordingly, holders of our ADSs may be unable to participate in our rights offerings and may experience dilution in their holdings.

In addition, the depositary of our ADSs has agreed to pay to ADS holders the cash dividends or other distributions it or the custodian receives on our ordinary shares or other deposited securities after deducting its fees and expenses. ADS holders will receive these distributions in proportion to the number of ordinary shares such holders' ADSs represent. However, the depositary may, at its discretion, decide that it is inequitable or impractical to make a distribution available to any holders of ADSs. For example, the depositary may determine that it is not practicable to distribute certain property through the mail, or that the value of certain distributions may be less than the cost of mailing them, or that the distribution requires certain governmental approval, such as requirement for registration or approval for currency conversion. In these cases, the depositary may decide not to distribute that property and ADSs holders will not receive that distribution.

*ADS holder will experience dilution when additional Class A ordinary shares or Class B ordinary shares are issued in settlement of restricted share units or upon exercise of options.*

ADS holders will experience dilution to the extent that additional Class A ordinary shares are issued upon settlement of restricted share units or exercise of outstanding options that we may grant from time to time. As of February 21, 2014, there were no Class B restricted share units outstanding, and there were 289,588 Class A restricted share units outstanding, with each such restricted share unit settleable upon vesting by the issuance of one Class A ordinary share.

*We may need additional capital and may sell additional ADSs or other equity securities or incur indebtedness, which could result in additional dilution to our shareholders or increase our debt service obligations.*

We may require additional cash resources due to changed business conditions or other future developments, including any investments or acquisitions we may decide to pursue. If our cash resources are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities or obtain a credit facility. The sale of additional equity securities or equity-linked debt securities could result in additional dilution to our shareholders. The incurrence of indebtedness would result in increased debt service obligations and could result in operating and financing covenants that would restrict our operations. We cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all.

*Substantial future sales of our ADSs or ordinary shares in the public market, or the perception that these sales could occur, could cause the price of our ADSs to decline.*

Additional sales of our ADSs or ordinary shares in the public market, or the perception that these sales could occur, could cause the market price of our ADSs to decline. As of February 21, 2014, there were 23,202,686 of our Class A ordinary shares and 82,490,000 of our Class B ordinary shares outstanding. As of February 21, 2014, there were no Class B restricted share units outstanding and there were 289,588 Class A restricted share units outstanding, with each such restricted share unit settleable upon vesting by the issuance of one Class A ordinary share. In addition, we may grant or sell additional options, restricted shares or other share-based awards in the future under our share incentive plan to our management, employees and other persons, the settlement and sale of which may further dilute our shares and drive down the price of our ADSs.



*We might be classified as a passive foreign investment company, which could result in adverse U.S. federal income tax consequences to U.S. holders of our ADSs or Class A ordinary shares.*

A non-U.S. corporation will be considered a passive foreign investment company, or PFIC, for any taxable year if either (i) at least 75% of its gross income is passive income or (ii) at least 50% of the value of its assets (based on an average of the quarterly values of the assets during a taxable year) is attributable to assets that produce or are held for the production of passive income. We expect that we will not be treated as a PFIC for U.S. federal income tax purposes for our current taxable year ending November 30, 2013. Our expectation is based on our current and anticipated operations and composition of our earnings and assets (including goodwill) for the 2013 taxable year, including the current and expected valuation of our assets based on the market price of our ADSs. However, we currently hold, and expect to continue to hold following this annual report, a substantial amount of cash, and the value of our other assets may be based in part on the market price of our ADSs, which is likely to fluctuate in the future (and may fluctuate considerably given that market prices of Internet and online game companies historically have been especially volatile). Furthermore, it is not entirely clear how the contractual arrangements between us and our consolidated variable interest entities will be treated for purposes of the PFIC rules. In addition, our actual PFIC status for any taxable year will not be determinable until the close of such taxable year. Accordingly, there is no guarantee that we will not be a PFIC for any taxable year. PFIC status depends on the composition of our assets and income and the value of our assets (including, among others, a pro rata portion of the income and assets of each regarded subsidiary in which we own, directly or indirectly, at least 25% (by value) of the equity interest) from time to time. If we were treated as a PFIC for any taxable year during which a United States holder held an ADS or a Class A ordinary share, certain adverse United States federal income tax consequences could apply to the U.S. holder. See "Taxation—United States Federal Income Taxation—Passive Foreign Investment Company" in Item 10 of this annual report.

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

##### *History and Development of the Company*

Our MMOG business began operations as a business unit within the Sohu Group in 2003. In June 2003, the Sohu Group launched its first MMOG, KO, which was licensed from a Korean developer. KO had limited acceptance in the Chinese market, and its operation was discontinued in November 2006 when the license expired. In October 2004, the Sohu Group launched BO, its second MMOG, which was licensed from a local independent game studio. In May 2007, the Sohu Group launched TLBB, its first in-house developed MMOG.

In 2007, the Sohu Group reorganized its MMOG business. As part of the reorganization, Changyou.com Limited was incorporated in the Cayman Islands on August 6, 2007 as an indirect wholly-owned subsidiary of Sohu.com Inc., to hold the MMOG business of the Sohu Group. Subsequently,

- Changyou.com (HK) Limited, or Changyou HK, was incorporated in Hong Kong on August 13, 2007 as a direct, wholly-owned subsidiary of Changyou. Changyou HK is the intermediate offshore holding company for our online game operations in China;
- Beijing AmazGame Age Internet Technology Co., Ltd., or AmazGame, was incorporated in the PRC on September 26, 2007 as a direct wholly-owned subsidiary of Changyou HK to undertake the technical support and product development functions of our online game operations; and
- Beijing Gamease Age Digital Technology Co., Ltd., or Gamease, was incorporated in the PRC on August 23, 2007 as our VIE, to operate our MMOG operations and to hold intellectual property and online game operating licenses and permits relating to our online game operations.

After the establishment of the above entities, Changyou, AmazGame and Gamease entered into various agreements with Sohu. Pursuant to these agreements, Sohu transferred to us, effective December 1, 2007, all of its assets and operations relating to its MMOG business unit, and we assumed all the liabilities associated with Sohu's MMOG business unit.

Trading in the ADSs offered in our initial public offering commenced on the NASDAQ Global Select Market on April 2, 2009.

In October 2009 and in August 2010, we established our PRC subsidiary Gamespace and our VIE Guanyou Gamespace, respectively, to operate certain of our new games.

In May 2010, Changyou HK acquired from ICE Entertainment Limited 100% of the equity interests in ICE Entertainment (HK) Limited, or ICE HK. ICE HK holds 100% of the registered capital of ICE Information and ICE Information controls the operation and management of Shanghai ICE through contractual arrangements. In May 2010, AmazGame, through its wholly-owned subsidiary Beijing Yang Fan Jing He Information Consulting Co., Ltd, or Yang Fan Jing He, acquired 50% of the equity interests in each of Shanghai Jingmao Culture Communication Co., Ltd, or Shanghai Jingmao, and Shanghai Hejin Data Consulting Co., Ltd, or Shanghai Hejin, which primarily engages in the cinema advertising business. In January 2011, Yang Fan Jing He acquired the remaining 50% of the equity interests in each of Shanghai Jingmao and Shanghai Hejin and became the sole shareholder of these two companies. In April 2012, in connection with an internal reorganization, Yang Fan Jing He acquired 100% of the equity interests in Beijing Changyou Jingmao Film & Culture Communication Co., Ltd., or Beijing Jingmao, from Shanghai Jingmao.





In May 2011, we, through our VIE Gamease, acquired 68.258% of the equity interests in Shenzhen 7Road for fixed cash consideration of approximately \$68.26 million, plus additional variable cash consideration of up to a maximum of \$32.76 million that was contingent upon Shenzhen 7Road's achievement of specified performance milestones through December 31, 2012. Shenzhen 7Road is primarily engaged in Web game development and operates our Web games Wartune and DDTank. On June 26, 2012, we completed the reorganization of Shenzhen 7Road into a Cayman Islands holding company structure, or the 7Road Reorganization, as follows:

- 7Road.com Limited, or 7Road Cayman, was incorporated in the Cayman Islands in June 2011.
- 7Road.com HK Limited, or 7Road HK, was incorporated in Hong Kong on July 6, 2011 as a wholly-owned subsidiary of 7Road Cayman.
- 7Road Technology, a WFOE, was incorporated in the PRC on December , 2011 as a wholly-owned subsidiary of 7Road HK.
- In June 2012, our indirect wholly-owned subsidiary Changyou Webgames (HK) Limited, or Webgames HK, received 68,258,000 ordinary shares of 7Road Cayman and the then four management shareholders of Shenzhen 7Road received an aggregate of 31,742,000 ordinary shares of 7Road Cayman.
- Also in June 2012, the then CEO of 7Road surrendered 5,100,000 ordinary shares of 7Road Cayman held by him with the intention that these shares would be added to the shares reserved by 7Road Cayman for grants of equity incentive awards under the 7Road.com Limited 2012 Share Incentive Plan, or the 7Road 2012 Share Incentive Plan.
- Upon completion of the 7Road Reorganization, we held 71.926% of the equity interests in 7Road. Also as part of the 7Road Reorganization, 7Road Technology, Shenzhen 7Road and the then shareholders of Shenzhen 7Road, which were our VIE Gamease and the then minority shareholders of 7Road, entered into contractual arrangements, or the VIE arrangements, with respect to ownership, disposition of ownership and control of Shenzhen 7Road, and 7Road Technology's provision of product development, technical support and marketing services to Shenzhen 7Road in return for payments from Shenzhen 7Road.

On June 5, 2013, we acquired all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders and, through our VIE Gamease, all of the equity interests in Shenzhen 7Road held by shareholders other than Gamease, for aggregate cash consideration of approximately \$78 million. As a result of the acquisition, 7Road Cayman became our indirect wholly-owned subsidiary and our VIE Gamease became the sole shareholder of our VIE Shenzhen 7Road. See "Major Shareholders and Related Party Transactions" in Item 7 of this annual report.

On December 15, 2011, we completed the acquisition from Sohu of certain assets and business operations associated with the 17173 Business for fixed cash consideration of \$162.5 million. Under our acquisition agreement with Sohu, net profits of \$1.3 million generated from our operation of the 17173 Business from December 16, 2011 to December 31, 2011 were for Sohu's benefit rather than ours. The 17173 Business operates the 17173.com Website, which is one of the leading game information portals in China. See "Major Shareholders and Related Party Transactions" in Item 7 of this annual report.

On September 24, 2013, we, through our VIE Guanyou Gamespace, entered into an agreement to acquire 100% of the equity interests in Doyo, which primarily engages in the game information business.

On November 19, 2013, we, through our wholly-owned subsidiary Heroic Vision Holdings Limited, or Heroic, entered into an investment agreement with Beijing Kunlun Tech Co., Ltd. and certain of its affiliates (collectively, the "Kalends Group"), pursuant to which TalkTalk limited, or TalkTalk, was incorporated in the British Virgin Islands and initially wholly-owned by the Kalends Group, RaidCall (HK) Limited, or RaidCall HK, was incorporated in Hong Kong as a wholly-owned subsidiary of TalkTalk, and Beijing Changyou RaidCall Internet Technology Co., Ltd., or Changyou RaidCall, was incorporated in the PRC as a wholly-owned subsidiary of RaidCall HK. The Kalends Group then transferred to RaidCall HK and Changyou RaidCall all of the assets associated with the RaidCall Business. On December 24, 2013, pursuant to the investment agreement, we acquired 62.5% of the equity interests, on a fully-diluted basis, in TalkTalk for cash consideration of \$ 47.6 million. Of the total consideration, we paid \$27.6 million to purchase from the Kalends Group a portion of the ordinary shares of TalkTalk held by the Kalends Group, and we invested \$20 million in newly-issued ordinary shares of TalkTalk. Also effective upon the closing of the transaction, 15% of the equity interests of TalkTalk on a fully-diluted basis were reserved for grants of equity incentive awards to key employees of the RaidCall Business and the Kalends Group continued to hold the remaining 22.5% of the equity interests on a fully-diluted basis.





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Our principal executive offices are located at East Tower, Jing Yan Building, No. 29 Shijingshan Road, Shijingshan District, Beijing 100043, People's Republic of China. Our telephone number at this address is (8610) 6861-3688. Our registered office in the Cayman Islands is located at 4th Floor, Willow House, Cricket Square, P O Box 2804, Grand Cayman KY1-1112, Cayman Islands. Our agent for service of process in the United States is CT Corporation System, 111 Eighth Avenue, New York, New York 10011.

### ***Business Overview***

We are a leading online game developer and operator in China as measured by the popularity of our MMOG TLBB and our Web games Wartune and DDTank, which we developed in-house. We engage in the development, operation and licensing of online games for PCs and mobile devices. This includes MMOGs, which are interactive online games that may be played simultaneously by hundreds of thousands of game players, Web games, which are played over the Internet using a Web browser, and mobile games, which are played on mobile devices and require an Internet connection. We also own and operate a number of Web properties and software applications for PCs and mobile devices (collectively referred to as "platform channels") related to games, including the 17173.com Website, one of the leading information portals for game players in China, the 37wanwan.com Website, a games portal that provides a collection of Web games to game players, and Raidcall, free social communication software that is used by professional and casual gamers. For the three months ended December 31, 2013, the games that we operate had approximately 25 million total average monthly active accounts, and our platform channels had approximately 149 million total average monthly active accounts.

TLBB is a popular martial arts MMORPG in China that is adapted from the popular Chinese martial arts novel "*Tian Long Ba Bu*," which means "*Novel of Eight Demigods*," written by the famous writer Louis Cha. Since TLBB's launch in May 2007, we have regularly developed new content and released game updates in the form of expansion packs for the game. TLBB has won various awards in China, including 2008 "Best Self-Developed Online Games (First Place)" and 2008 and 2009 "Most Liked Online Games by Game Players (First Place)" awards at the China Digital Entertainment Expo and Conference, or ChinaJoy. Its expansion packs, TLBB2, TLBB3 and New TLBB, won the 2010 "Most Liked Online Games by Game Players" award, the 2011 "Best Self-Developed Online Games" award, and the 2013 "Most Liked Online Games by Game Players" award, respectively, at ChinaJoy. TLBB was chosen as one of the 2012 "Most Liked Online Games by Game Players" at ChinaJoy. TLBB is currently licensed to third-party operators in Vietnam, Taiwan, Hong Kong, Malaysia and Thailand. We also operate a modified version of TLBB in the U.S.

DDTank is a popular 2D multi-player, combat and role-playing Web game in China. Game players control avatars to compete with other game players. Avatars can earn or buy various weapons, potions, magic rings, rockets and other items to increase competitiveness and enhance the game experience. Since DDTank's launch in March 2009, we have regularly released updates and more significant enhancements for the game. DDTank has won numerous game awards, including the "Baidu Outstanding Web Game" award in 2010 and 2012 and "One of the Top Ten Favorite Web Games" by SAPPRFT in 2010 and 2011. DDTank was also the most searched-for casual Web game on Baidu.com for the 12 months ended each of June 30, 2012 and June 30, 2013, according to Baidu. We also jointly operate DDTank with third-party operators overseas. DDTank has been launched in 15 different language versions.

Wartune is a popular 2.5D role-playing and quasi real-time strategy Web game launched in December 2011 in China. Wartune is set in a mythical western universe where players build their own kingdoms in a virtual world where they must fight against a demonic race by developing their own villages and armies. Wartune won the "Baidu Outstanding Web Game" award in 2012 and the "Most Liked Web Games by Game Players" award at ChinaJoy in 2013. We also jointly operate Wartune with third-party operators overseas. Wartune has been launched in 15 different language versions.

We have several MMOGs, Web games and mobile games in our pipeline with different graphic styles, themes and features to appeal to different segments of the online game player community. Games in our pipeline, include, among others, a self-developed MMOG, YZZX; three licensed MMOGs, Echo of Soul, Asta, and Fantasy Frontier Online; two self-developed Web games, JY and SZHG; and several jointly-developed mobile games adapted from literary or other copyrighted works that we directly own or have acquired the exclusive rights to use from third-parties.

We also own and operate the 17173.com Website, a leading game information portal in China that provides news, electronic forums and other information services on online games to game players. The 17173.com Website was launched in 2000 as the first online game information portal in China, and is a leading online destination for game players seeking information on games and feedback from other players on the site's message boards. With over 750 game zones and tens of millions of monthly unique visitors supported by alliances with many thousands of Internet cafes, the 17173.com Website is one of the largest game information and community Websites in China and is widely recognized as a market leader among game Websites in China, with strong expertise in running the Website, building a game community and developing relationships with advertisers in the online game industry. As a result, the 17173.com Website is the marketing platform of choice for many online games, including our own. In addition, experienced game editors of the Website review and critique our games prior to launch, and we use the feedback received to improve the game quality of our games. We generate online advertising revenues from providing advertising services to third-party advertisers on the 17173.com Website. The 17173.com Website has won "Best Game Media" award for ten consecutive years from 2004 to 2013 at the Annual Game Industry Awards Gala.



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We also own and operate in China and overseas other game-related platform channels, including the 37wanwan.com Website, a games portal that provides a collection of Web games to game players; Raidcall, which is free social communication software that is used by professional and casual gamers; and other software applications that serve as access points to the 17173.com Website. The platform channels, as a whole, serve various needs of our game players and help us reach more game-player communities and conduct cross-promotions of our games and services, which in turn improve user loyalty.

Sohu.com Inc., our controlling shareholder, has operated a leading Chinese Internet portal, www.Sohu.com, since 1998. We have benefited from Sohu's strong brand recognition in China and large user base. Sohu's trusted brand name in China provides us with a broad marketing reach. By marketing across Sohu's Web domains and taking advantage of the Sohu Group's single-user ID system that provides easy access to our games, we believe we have been able to tap into Sohu's large user base to drive new users to our games. We intend to continue to leverage our relationships with Sohu in the development, marketing and operation of our games.

We operate our current games under the item-based revenue model, meaning game players can play our games for free, but may choose to buy prepaid game cards that are used to pay for virtual items, which are non-physical items that game players can purchase and use within a game, such as gems, pets, fashion items, magic medicine, riding animals, hierograms, skill books and fireworks, to enhance the game-playing experience. For games that we operate, we mainly directly sell prepaid game cards to regional distributors and our game players in China through our online sales platform. Regional distributors sub-distribute prepaid game cards purchased from us to numerous retail outlets, including Internet cafés and various Websites, newsstands, software stores, book stores and retail stores. For games that we license to third-party operators, the licensee operators pay us an upfront license fee and we have revenue sharing rights over the duration of the license.

We continually collect feedback from our game players through multiple channels. Our product development team and our game operations team work closely together, allowing us to translate game player feedback into game updates and expansion packs in a timely manner. We typically release expansion packs, which are software packages that contain significant upgrades and improvements to a game based on the existing game's framework, every few months or as regularly as necessary based on game players' feedback, market demand and other factors. These upgrades may include new game content such as storylines, characters, tasks, maps and virtual items. We also update our games on a weekly basis with interim enhancements. We believe that such expansion packs and regular updates improve the game-playing experience and help to maintain the interest level of our game players, thereby helping us to extend the lifespan of our games.

Our revenues grew from \$484.6 million for the year ended December 31, 2011 to \$623.4 million for the year ended December 31, 2012, and to \$737.9 million for the year ended December 31, 2013, and our net income attributable to Changyou.com Limited grew from \$245.5 million for the year ended December 31, 2011 to \$282.4 million for the year ended December 31, 2012, and to \$268.6 million for the year ended December 31, 2013.

### ***Our Games***

We design, develop and operate online games, including MMOGs, Web games and mobile games. All of our games are operated under the item-based revenue model, where game players can play our games for free, but can also purchase virtual items to enhance their game-playing experience. Our games vary in theme and span a number of genres, and attract a diverse community of game players. Our games also connect players with each other and with their friends who share a common interest in playing our games.



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### *Games in Operation*

We currently operate 11 MMOGs, three Web games, and several mobile games. Key games that are currently in operation include TLBB; DDTank; Wartune; the Blade Online series, which consists of BO and BH2; DMD; DSHH; Dou Po Cang Qiong; Wartune (mobile version) and TLBB (mobile version). Descriptions of these games are provided below:

#### MMOGs

##### *Tian Long Ba Bu (TLBB)*

Genre: 3D martial arts role-playing

Game Type: MMOG

Initial Launch Date: May 2007

Regions: China, Vietnam, Taiwan, Hong Kong, Malaysia, Thailand and North America



TLBB is an in-house developed 3D martial arts MMORPG adapted from the popular Chinese novel, “*Tian Long Ba Bu*,” which means “*Novel of Eight Demigods*.” The missions and activities of the game generally follow the storyline of the novel, which we have adapted to add new features and characters. TLBB features a combination of martial arts-style-fighting and community-building among its game players, which we believe holds strong appeal for game players. Players can choose from ten classes, several occupations and over 100 skills to build up their in-game characters and train their characters by participating in missions, duels, team fights, and large-scale cross-server group battles.

We typically release updates for TLBB once or twice a week and more significant enhancements in the form of expansion packs every few months. We have developed 27 expansion packs since its launch, including four major expansion packs “TLBB2,” “TLBB3,” “Shen Bing Hai Yu” and “New TLBB” that were released in April 2010, October 2011, October 2012 and October 2013, respectively. TLBB2, TLBB3 and New TLBB won the 2010 “Most Liked Online Games by Game Players,” the 2011 “Best Self-Developed Online Games,” and the 2013 “Most Liked Online Games by Game Players” awards, respectively, at ChinaJoy. In 2012, TLBB was named as one of the “Most Liked Online Games by Game Players” at ChinaJoy.



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*Blade Online series*

Genre: 2.5D martial-arts style fighting role-playing

Game Type: MMOG

Initial Launch Date: *Blade Online (BO)* in October 2004; *Blade Hero II (BH2)* in September 2009

Regions: China



The Blade Online series consists of two 2.5D martial-arts style fighting MMORPGs, Blade Online, or BO, which we licensed from a third party, and Blade Hero 2, or BH2, which is a sequel of Blade Online. Both games are martial arts-style fighting games set to the backdrop of a Chinese myth. In BO, game players can set their own rules for in-game fighting and take on various roles in the game, including a human, an evil spirit or an immortal. Each role has different skill sets that can be learned and improved by completing different tasks. BH2 incorporates popular features of BO as well as new features such as new maps, new characters, new fighting techniques and additional team-combat functions to give players a more intense and realistic fighting experience. The game also includes upgrades to some of the community features found in BO, such as an auto-navigation system, an improved mission tracking system and enhanced visual effects.



*Duke of Mount Deer (DMD)*

Genre: 3D cartoon-style martial arts role-playing

Game Type: MMOG

Initial Launch Date: July 2011

Regions: China, Taiwan, Indonesia and Hong Kong



DMD is an in-house developed 3D martial arts MMORPG based on Louis Cha’s final novel “Duke of Mount Deer.” The game recreates Louis Cha’s final martial arts world with fresh and stunning cartoon-style graphics, supported by a proprietary 3D animation engine. The game is defined by an open story line populated with classic heroes. DMD combines four different types of combat: Magic, Taoism, Martial arts and Firearms. Each character can choose up to three different job classes and command up to five different kinds of pets at the same time, allowing a single player to set up an exclusive adventure group. Using a proprietary server technology that allows connected gameplay across different servers, gamers can enter parallel worlds to experience new adventures with friends. In addition, users on two different servers can form alliances against competing teams on other servers, allowing large communities of players to meet, network and compete with each other online. DMD won the 2011 “Best 3D Online Game” award at ChinaJoy, and was named as one of the “Best Online Games” at the Annual Game Industry Awards Gala in 2013.





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*Da Hua Shui Hu (DHS)*

Genre: 2D Q-style turn-based role-playing

Game Type: MMOG

Initial Launch Date: March 2010

Regions: China



DHS is a 2D Q-style, turn-based MMORPG, which we licensed from a third party. The game is based on a story from one of the four great classical novels of Chinese literature “*Outlaws of the Marsh*,” which is about the adventures of 108 heroes in the Northern Song dynasty. Through its cartoon graphics and humorous twists on characters and plots, the game provides an amusing and entertaining take on heroic tales from the classic Chinese novel. DHS won the 2010 “Best Q-Style Online Game” award at ChinaJoy.



*Dou Po Cang Qiong*

Genre: 2.5D fantasy martial arts role-playing

Game Type: MMOG

Initial Launch Date: April 2013

Regions: China



Dou Po Cang Qiong is an in-house developed 2.5D fantasy martial arts MMORPG that is adapted from a popular Chinese online literary work of the same name. Players can explore the fantasy world and relive the scenes described in the novel with their friends. Players can also upgrade their martial arts skills and form teams to compete with other players to determine their standing in the martial arts world.



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Web Games*DDTank*

Genre: 2D multi-player, combat and role-playing

Game Type: Web game

Initial Launch Date: March 2009

Regions: China and 14 other countries and/or regions



DDTank is a 2D multi-player, combat and role-playing Web game developed by 7Road. Players use keyboards to control avatars to compete with other game players. Avatars can earn or buy various weapons, potions, magic rings, rockets and other items to increase competitiveness and enhance the game experience. Players have many options to customize their avatars. The game features stunning scenery and battle scenes, vivid special effects and thousands of costumes and accessories. Players socialize with friends and others through battles, exchanging strategy advice, sending virtual gifts, chatting and even getting married or divorced.

We introduced significant enhancements to the game in the new version DDTank II in June 2012. DDTank II introduced new features, including pet animals to help game players complete challenges and win shooting competitions. Players can enhance their pets' powers by visiting a virtual farm and plowing, planting and harvesting crops to feed their pets. DDTank II also adds more in-game challenges and promotional activities to give players more opportunities to buy or earn game coins.

DDTank has been launched in 15 different language versions (English, Spanish, French, Vietnamese, Japanese, Russian, Korean, Arabic, Thai, Malay, Indonesian, Portuguese, Turkish, Traditional Chinese and Simplified Chinese).

DDTank has won numerous game awards, including the "Baidu Outstanding Web Game" award in 2010 and 2012 and "One of the Top Ten Favorite Web Games" by SAPPRFT in 2010 and 2011. DDTank was also the most searched-for casual Web game on Baidu.com for the 12 months ended June 30, 2012 and June 30, 2013, according to Baidu.



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*Wartune (also known as Shen Qu)*

Genre: 2.5D quasi real-time strategy and role-playing

Game Type: Web game

Initial Launch Date: December 2011

Regions: China and 14 other countries and/or regions



Wartune is a 2.5D quasi real-time strategy and role-playing Web game set in a mythical western universe developed by 7Road. Wartune features an engaging storyline, a touch of fantasy, and memorable characters. Players build their own kingdoms in a virtual world where they must fight against a demonic race by developing their own villages and armies. The unique feature differentiating Wartune from traditional turn-based strategy games is that our game play is in quasi real-time. Players play simultaneously, making combat smoother, eliminating delays and increasing game play excitement as situations develop real-time on the battlefield.

In addition to mainland China, we jointly operate Wartune in Brazil, Canada, Germany, Hong Kong, Macau, Malaysia, South Korea, Taiwan, Thailand, Turkey, the United States, and Vietnam, and in 15 different language versions (English, German, Korean, Portuguese, Thai, Turkish, Vietnamese, Polish, Russian, French, Spanish, Italian, Indonesian, Traditional Chinese and Simplified Chinese).

Before its launch in December 2011, Wartune was among the games given a 2012 “Most Anticipated Web Games” award by the Internet Society of China. After its launch, Wartune won the “Baidu Outstanding Web Game” award in 2012, and the “Most Liked Web Games by Game Players” award at ChinaJoy in 2013.





Mobile Games

TLBB (mobile version)

Genre: Battle card and strategy

Game Type: Mobile game

Initial Launch Date: October 2013

Regions: China



TLBB (mobile version) is a battle card and strategy game that is adapted from Louis Cha's popular martial arts novel of the same name. Players experience classic plotlines from the original novel and must collect cards of various martial arts characters to form teams of a maximum of six cards and strategize on team composition and the placement of cards in order to compete effectively with other players and advance in the game. The game was named as one of the "Top 10 among the Best Free iPad Apps" and as one of the "Top 10 among the Best Free iPhone Apps" in China in the first week of its launch.





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*Wartune (mobile version)*

Genre: Role-playing and combat game

Game Type: Mobile game

Initial Launch Date: September 2013

Regions: China



Wartune is a role-playing and combat mobile game that was adapted from our popular Web game of the same name, which we jointly developed with third party developers. Wartune was designed with a unique fighting system, which allows players to enhance their combat effects and release powerful skills by pressing certain keys and/or repeating strokes on a touchscreen mobile device in order. Compared with traditional turn-based games, this fighting game is more intense and exciting and requires players to react in real-time during gameplay.



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### *Our Game Pipeline*

We have in the pipeline several MMOGs, Web games and mobile games of different graphic styles, genres and features. Games in our pipeline, include, among others, a self-developed MMOG, YZZX; three licensed MMOGs, Echo of Soul, Asta, and Fantasy Frontier Online; two self-developed Web games, JY and SZHG; and several jointly-developed mobile games adapted from literary or other copyrighted works that we directly own or have acquired the exclusive rights to from third-parties. We intend to operate all of these games under the item-based revenue model.

#### MMOGs

*Yong Zhe Zhi Xin (YZZX)*

Genre: 2.5D fantasy role-playing

Game Type: MMOG

Expected launch date: 2014



YZZX is a 2.5D fantasy role-playing MMOG featuring Korean-style graphics, which we developed in-house. In the game settings, players are allowed to switch between 2.5D and 3D display modes. For movement, the left mouse button allows players to move a character or attack a target, while the WASD keys provide further control. The game offers three races, including humans, elves and orcs, and two character classes under each race. Users can toggle between two battle stances under each class in order to deal with different battle conditions.



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*Asta*

Genre: 3D Asian fantasy role-playing

Game Type: MMOG

Expected launch date: 2014



Asta is a 3D Asian fantasy role-playing MMOG licensed from a Korean game studio. It incorporates styles from multiple Asian cultures, including those of South Korea, Japan, and China. Players are divided into two clans and complete missions and participate in large-scale siege battles.



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*Echo of Soul*

Genre: 3D fantasy role-playing

Game Type: MMOG

Expected launch date: 2014



Echo of Soul is a 3D fantasy role-playing MMOG set against a backdrop of Norse mythology. The game provides vast excitement through grand battles, high-quality graphics and a unique soul collecting system.





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*Fantasy Frontier Online*

Genre: 3D Western fantasy role-playing

Game Type: MMOG

Expected launch date: 2014



Fantasy Frontier Online is a 3D Western fantasy role-playing MMOG licensed from a game studio in Taiwan. The game features a Japanese animation style and offers a unique gaming experience with a dual role model, pets system and impressive plotlines. It allows players to choose a primary weapon from eight weapons, all of which have unique skills.





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Web Games*Shen Zhi Huang Guan*

Genre: 2D side-scrolling real-time battle

Game Type: Web game

Expected launch date: 2014



Shen Zhi Huang Guang is a 2D side-scrolling real-time battle Web game set in a Western fantasy world. The game uses Multiplayer Online Battle Arena (“MOBA”) mode and allows players to lead generals and soldiers to protect the last human castle against the invasion of demon armies.



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*Jian Ying*

Genre: Fantasy role-playing adventure

Game Type: Web game

Expected launch date: 2014



Jian Ying is a fantasy role-playing adventure Web game with only female characters. Players can work together to create different battle forms to combat enemies. Battle is accompanied by realistic sound effects and human voices for lead characters in the game.



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Mobile Games

*DDTank (mobile version)*

Genre: role-playing and shooting game

Game Type: Mobile game

Expected launch date: 2014



DDTank (mobile version) is a multi-player, combat and role-playing mobile game adapted from our popular Web game of the same name. The mobile game features many of the most popular features from the original DDTank Web game.



**Virtual Items Revenue Model**

All of our games are operated under the item-based revenue model, where game players play our games for free but can purchase virtual items. Through virtual items, players are able to enhance or personalize their game environments or game characters, accelerate their progress in our games and share and trade with friends. We generate revenue through the sale and consumption of such virtual items. The major categories of virtual items we sell to generate revenues are gems, pets, fashion items, weapons, magic medicine, riding animals, hierograms, materials, skill books and fireworks. We determine the price of virtual items based on the demand or expected demand for such virtual items. We may change the pricing of certain virtual items based on their consumption patterns.

**Example of a virtual store in TLBB**



For players who choose to purchase virtual goods, we deliver enhanced gameplay experiences and benefits, such as:

*Accelerated Progress.* Many of our games offer players the option to purchase items that can accelerate their progress in the game and increase their capabilities, so that they level up more quickly and compete more effectively against others in the game. While we sell many items that accelerate progress in our games, we monitor and carefully balance the disparity in capabilities between paying and non-paying game players to avoid discouraging non-paying game players and to keep the game challenging and interesting for paying game players.

*Enhanced Social Interaction.* We use a variety of virtual items to promote interaction and to facilitate relationship-building among game players in our games.

*Personalized and Customized Appearance.* Many of our games offer players the option to purchase decorative and functional items to customize the appearance of their characters, pets, vehicles, houses and other in-game possessions to express their individuality.

*Gifts.* Many of our games offer players the option to purchase gift items to send to their friends. Examples of gift items include decorative items and time-limited items for special holiday events and festivals, such as Valentine’s Day, Spring Festival (Chinese New Year) and Christmas.





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### Community Experience in Our Games

The community design of our games is at the core of how our players experience our games. Our games encourage players to quickly connect to their friends when they start a game and to build and enhance these relationships throughout the game experience. Examples of community gameplay in TLBB are detailed below.

*To share information and chat with friends..*

*To easily connect with friends*



### Game Development and Enhancement

As of December 31, 2013, we had 3,139 product development personnel, which include a core product development team that is responsible for developing new online games, including MMOGs, Web games and mobile games, and a dedicated product development team that is responsible for developing game enhancements and expansion packs for each of our games in operation. We believe that such enhancements improve our games' appeal and extend our games' lifespan. We intend to expand our product offerings by continuing to develop additional online games in-house and continuing to license online games from third parties.

#### New Game Development

We have in-house capabilities that allow us to develop quality online games efficiently and in response to constantly changing market demands and trends. Our game development process generally includes the following key steps:

- **Concept generation.** Our design department takes the lead in generating game development ideas based on the latest trends in game player preferences. We recruit game players into our design team to ascertain popular trends among our game players and on the Internet. We also encourage all of our employees to suggest creative ideas and concepts for game development.
- **Detailed proposal.** Upon management's approval of the new game concept, the design department prepares a detailed proposal that sets preliminary storylines, game characters, estimates of costs and target markets.
- **Development plan.** After the completion of technical review of the proposal, a project team consisting of our software programmers, platform technicians, media specialists, design staff and graphics artists work together to set the technical criteria for development of the game, and then formulate a game development plan with development milestones.
- **Design, style and story concepts.** Based on the game development plan, our graphics artists determine the style of the new game and design game characters; our game designers develop the game story and define game environments; and our program developers develop both the server-end software and the user-end software modules.
- **Internal reviews.** Mid-term management reviews take place upon the completion of each milestone of the development plan. Concurrently, our testing department tests the accuracy and completeness of the development, and our marketing department initiates marketing campaigns according to the development milestones.
- **Technical closed beta testing, closed beta testing and open beta testing.** We conduct technical closed beta testing to work out technical issues and eliminate technical problems in the game engine and system. Thereafter, we conduct closed beta testing to test and work out technical issues in game features and make adjustments to the in-game economic system. Lastly, we conduct open beta testing to test the operation of new games under open market conditions and introduce new games to players.





Our games are developed through coordination among teams of program developers, game designers and graphic artists. We try to design each of our games to cater to different audiences to grow our overall player base rather than merely shifting players from one game to another. At each stage of a new game's development, we rely on our quality control department to ensure the game's quality and playability.

#### *Existing Game Enhancement*

We derive many of our game development and enhancement ideas from our game players by maintaining multiple channels whereby we obtain our game players' ideas and feedback. These include online surveys, online discussion forums, in-game instant messaging, online customer service and a link to a form for feedback within our games. We use this information not only to create new games with the same quality of design, content and programming, but also to enhance existing games that we have either developed in-house or licensed from third parties.

We typically release game updates for our games once or twice a week and more significant enhancements in the form of expansion packs every few months or as regularly as necessary based on game players' feedback, market demand and other factors. Our expansion packs typically include features such as new territories, themes, tasks, characters, virtual items and other enhanced features. After testing, the game updates and expansion packs are typically distributed electronically through a game Website hosted by us or by third parties. We have found that expansion packs effectively increase game players' interest in the game and enhance the game-playing experience by keeping the game-playing experience fresh even for long-time game players. We believe that the expansion packs help us to maintain game player loyalty, and in turn extend the lifespans of our games.

#### *Access to our Games*

Our game players typically access our games on personal computers, mobile phones, tablets and other hand-held devices connected to the Internet or at Internet cafés. In order to access our MMOGs, our game access software must be installed in the computer being used. Game players using personal computers and Internet café operators can typically download our game access software, interim updates and expansion packs directly from our official game Website. Game players can access our Web games on their browser using popular third-party plug-ins. Game players can also access our mobile games by downloading our mobile game applications from third-party mobile stores or our official game Website.

#### *Sales and Distribution*

For games that we operate, we directly sell game points to our game players through our online sales platform. We also have developed a sales and distribution system to sell and distribute our prepaid game cards in China.

#### *Third-Party Distributors*

We directly sell prepaid game cards in virtual form to a range of regional third-party distributors and our game players in China through our online sales platform. Regional distributors sub-distribute prepaid game cards purchased from us to numerous retail outlets, including Internet cafés and various Websites, newsstands, software stores, book stores and retail stores, as well as through various online channels, and telecommunications service providers. We typically collect payment from our distributors upon delivery of our prepaid game cards.

We generally enter into distribution agreements with our distributors of prepaid game cards for one-year terms. Our distribution agreements contain both pre-set sales targets and pre-set penetration targets, whereby distributors are required to sell our prepaid game cards in a minimum number of Internet cafés in its designated sales territory. We also require that each distributor work closely with our marketing team and support its activities. Our distribution agreements are not exclusive, and do not prohibit our distributors from working with our competitors.

#### *Direct Sales*

Game players can purchase game points and charge them to their accounts directly. To do this, they log into their accounts from the game. From the account link, game players can choose to either pay from their bank accounts or through other payment methods, including third-party online payment platforms. We provide discounts to game players who charge their accounts directly. Transaction costs also apply to the use of third-party online payment platforms.

For games that we license to third-party operators, we rely on third-party operators and their distributors to sell prepaid game cards to game players. The licensee operators pay us an upfront license fee and we have revenue sharing rights over the duration of the license.

### **Marketing**

For games that we operate directly, we have a three-pronged marketing and promotion strategy, which includes online advertising, off-line promotions and traditional media. We use different methods to target different demographic groups of game players.

With respect to online advertising, we are able to leverage our game information portal, the 17173.com Website, and game clients to promote our games. In addition, we are able to leverage our affiliation with Sohu, and aggregate Sohu's large user base to our games by advertising on Sohu's various Websites, which typically provide a direct link to our games. We also advertise on a variety of Websites, including on Internet café homepages and game portals. In addition, we use in-game promotional events 24 hours a day, seven days a week. We also create events to rally current and new game players through event-related features, such as offering special holiday edition virtual items to enhance game player participation at holiday time.

We also use a variety of physical, offline promotional events, including Internet café events, free trial plays, posters, game players' gatherings, "freshmen" (or new game player) incentives and the giving away of promotional souvenirs. We have found that these promotional events offer good exposure to targeted customers at a lower cost.

With respect to traditional media, we focus our marketing efforts on print advertisements in magazines that target our game player base and outdoor multimedia, including cinema advertisements, closed circuit television advertisements on buildings and in elevators. In addition, we are able to leverage our cinema advertising resources to promote our games.

For games that we license to or jointly operate with third-party operators, we rely on the third-party operator to promote our games.

For software applications that we develop, we carry out marketing through advertising on a variety of Websites, including using online advertisement networks, search engines and pre-installation of our software applications on PCs and/or mobile devices.

### **Customer Service**

For games that we operate directly and games that we jointly operate, we provide high-quality customer service and are responsive to our game players' needs. Our game players can seek our customer service support via phone or submit their feedback online 24 hours a day, seven days a week. In addition, we have a physical service center in Beijing, which is open to walk-in game players during normal business hours. We currently have around 237 dedicated customer service representatives, many of whom are online game enthusiasts with a deep understanding of game players. We have dedicated supervisors to monitor our service quality.

For games that we license to third-party operators, we rely on the third-party operator to provide customer service.

Feedback collected by our customer service team and by third-party operators that license our games is important to the integration of our product development and game operations teams. The information collected by our customer service team forms the basis of our feedback database, which helps us design changes, upgrades and expansion packs for our games. See "—Game Development and Enhancement."

### **Publishing**

#### *Games We Licensed from Third Parties*

We licensed rights to operate and further develop some of our MMOGs from their respective developers, with exclusive rights to operate such games in China. Below is a list of the primary MMOGs that we currently operate that are licensed from third parties.

We licensed BO from a local independent game studio in 2003. Under our existing licensing arrangement, we have the exclusive right to operate and further develop BO in China. We paid a one-time license fee in 2004 and we paid royalties until June 30, 2008 based on the revenues from the game. We are not required to pay any royalties starting from July 1, 2008. In 2007, we obtained the rights to the source codes of BO, and we own all enhancements and developments we make to BO.

We licensed DHSH from a local independent game studio in September 2009. Under the licensing arrangement, we have an exclusive right to operate DHSH in China. We paid upfront licensing fees and we pay additional licensing fees based on the game achieving performance milestones and royalties based on the revenues from the game.



We licensed several games, including Asta and Echo of Soul from independent game studios in Korea and Fantasy Frontier Online from an independent game studio in Taiwan, in 2013. Under the licensing arrangements, we have exclusive rights to operate these games in China. We paid up-front licensing fees and we pay additional licensing fees based on the games' achieving performance milestones and royalties based on the games' revenues.

#### *Rights from Third Parties to Game Titles and Characters*

Under the existing license agreements with Louis Cha, the author of the novels "*Tian Long Ba Bu*" and "*Duke of Mount Deer*," we have the exclusive right in China to adapt these two novels into online games and to operate such games, including the right to use the title of the novels and the name of the characters. We also have the non-exclusive license to operate, and the non-exclusive right to license the right to operate, the games adapted from these novels outside of China. Additionally, we secured the rights to adapt ten martial arts novels written by Louis Cha, including Tian Long Ba Bu, into mobile games. If we wish to continue to operate and license these games using the titles and character names from these novels after the expiration of the terms of these license agreements, we will need to renew the license agreements.

Under the existing licensing agreements with Tian Can Tu Dou, the author of the novel "*Dong Po Cang Qiong*," we have the exclusive right in China to adapt this novel into MMO games and to operate such games, including the right to use the title of the novel and the names of the characters.

#### *Licensing of Our Games*

We license the rights to operate TLBB, DMD and Tao Yuan, among others, in overseas markets. We currently license TLBB to third-party operators in Taiwan, Hong Kong, Vietnam, Malaysia, and Thailand; DMD to third-party operators in Taiwan and Indonesia; and Tao Yuan to third-party operators in Taiwan and Thailand. Under our licensing arrangements with the overseas operators, the licensee operators pay us an upfront license fee and we have revenue sharing rights over the duration of the license. The licenses are typically for a term of one to three years. We provide updates and expansion packs to the licensed game, typically after we launch such updates and expansion packs in China. The licensees are responsible for all other operating services and costs, including costs related to customer service and leasing and maintenance of servers.

#### *Joint Operation of Web Games with Third-party Platforms*

We jointly operate our Web games, such as our in-house developed Wartune and DDTank, with third-party joint operators through third-party platforms, which offer the games to users in China and overseas markets. Our domestic and overseas Web game revenues from joint operations consist of ongoing revenue-sharing payments and, under certain joint operation arrangements, a license fee. Certain of the joint operators pay us a license fee for the exclusive right to operate the games in specified geographic areas, upon achievement of certain performance milestones from their operation of the games, or to be among a selected few who will have the initial right to jointly operate the new games in China during a specified period after their launch ahead of other joint operators. The ongoing revenue-sharing payments are generally determined based on the amounts charged to game players' accounts. We typically receive ongoing revenue-sharing payments on a monthly basis. The joint operation agreements for the games in China are typically for a term of one year and the overseas joint operation agreements are typically for a term of one to three years.

#### *Service Offerings to Online Advertisers*

We offer various products and services (such as game news, game tutorials, discussion forums and other services) to game players in China, and provide advertising services to advertisers on the 17173.com Website. The 17173.com Website enjoys a strong competitive position as one of the leading game informational portals in China. Our offerings enable advertisers to post their advertisements in different forms, including text, rich media and video advertisements. Our online advertising products include, among other things, banners, links, logos, buttons and stream advertisements placed on our Websites and sponsorships that typically focus on a particular event or a particular Website area. We charge most advertisers on a time basis with fixed fees. We also adopted the Cost Per Impressions pricing model to cater to different advertisers, and particularly small-sized advertisers. Our standard advertising charges vary depending on the terms of the contract and the advertisement's location within the 17173.com Website. Discounts from standard rates are typically provided for higher volume, longer-term advertising contracts, and may be provided for promotional purposes.

We mainly rely on advertising agents for the selling of advertisements on 17173.com Website. During the year ended December 31, 2013, there were a total of approximately 150 companies advertising on the 17173.com Website. Our end customers include leading online game companies in China, as well as independent game studios.



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### *Other Service Offerings*

We sell pre-film cinema advertising slots, which are advertisements shown before the screening of a movie in a cinema theatre, to advertisers. Most of the advertisements are in the form of video advertisements. We sign contracts with individual cinema theatres and film production companies for the rights to sell their pre-film cinema advertising slots. These contracts are for an average period of two years. As of December 31, 2013, we had the right to sell pre-film cinema advertising slots at approximately 300 cinema theatres in China.

We charge most advertisers on a per-advertising slot basis or on a pre-determined period basis with fixed fees. Our standard prices for advertising slots vary depending on the location of the cinema theatre. Discounts from standard rates are typically provided for longer-term advertising contracts, and may be provided for promotional purposes.

### *Intellectual Property and Proprietary Rights*

We regard our intellectual property and proprietary rights as critical to our success. We rely on trademark and copyright law and trade secret protection, and intend to rely on PRC patent law if our currently pending PRC patent applications are approved, to protect our intellectual property rights. We enter into non-competition and confidentiality and/or license agreements with our employees, customers, partners and others to protect our intellectual property rights. Our employees are generally required to enter into agreements under which they undertake to keep confidential all information related to our methods, business and trade secrets during and for a reasonable time after their employment with us. In addition, we fragment our source codes so that no one employee, other than the Chief Operating Officer, has access to our entire source codes for a game. Product development personnel are only given access to the specific portions of the source codes that they need to work with at a particular time. In addition, all of the computers used by our game development personnel are closed circuit and do not have access to the Internet, so that we can protect our source codes and other proprietary information from being emailed out of our closed circuit system and misappropriated. However, we cannot guarantee that our measures to protect our intellectual property are sufficient. See “Risk Factors—Risks Related to Our Business and Our Industry—We may need to incur significant expenses to enforce our proprietary rights, and if we are unable to protect such rights, our competitive position and financial performance could be harmed” in Item 3.

We are the registered owner of 195 software copyrights and 362 fine arts work copyrights in China, each of which we have registered with the National Copyright Administration of the PRC or Guangdong Copyright Administration. We have registered with the NTSC UniTrust Time Stamp Authority in China the ownership rights to 911 fine arts work copyrights.

We are the registered owner of 391 domain names that we use in connection with the operation of our business, including our official Changyou Website, changyou.com and 17173.com. We also license the right to use certain of Sohu’s domain names, which we will continue until Changyou develops independent brand recognition, at which time we plan to phase out our use and licenses of certain of Sohu’s domain names.

We are the registered owner of 403 registered trademarks and have applied for the registration of another 1,908 trademarks in the PRC, including those related to our company name and our online games and other businesses. We are the registered owner of 123 registered trademarks and have also applied for 60 trademarks in countries and regions such as Taiwan, Hong Kong, the United States, Europe, Japan, Malaysia, South Korea, Thailand, Turkey and Vietnam relating to our company name, and our online games and other businesses. We have registered four trademarks in Taiwan and six trademarks in the European Union relating to TLBB, two trademarks in Taiwan and three in Japan relating to DMD, and 15 trademarks in countries and regions such as the European Union, Japan, Hong Kong and Taiwan relating to DDTank. However, we cannot assure you that we will be able to obtain the trademarks we have applied for. See “Risk Factors—Risks Related to Our Business and Our Industry—We may need to incur significant expenses to enforce our proprietary rights, and if we are unable to protect such rights, our competitive position and financial performance could be harmed” in Item 3.

We have 29 patent applications pending in the PRC which are related to the design of our games and technology intended to enhance the functionality of our games, but these patent applications may not be approved. See “Risk Factors” for discussions of various risks relating to intellectual property.

### *Technology Infrastructure*

We have built a reliable and secure network infrastructure to fully support our operations. As of December 31, 2013, we maintained approximately 9,317 servers related to our online game business, located in Internet data centers in 11 major cities in China, with the capacity to accommodate up to 7.9 million concurrent game players, and a sufficient amount of connectivity bandwidth to maintain such service. In order to enhance our game players’ experience and minimize the impact of cross-region connections, we have located our game servers in a number of regions throughout China, enabling our game players to play our games by connecting to the nearest servers located in their region without needing to exchange data across the national backbone network.



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We have technical support employees to maintain our current technology infrastructure and develop new software features to further enhance the functionality of our management and security system. We monitor the operation of our server network 24 hours a day, seven days a week. Our remote control system allows us to track our concurrent online users in real time, and discover and fix problems in the operation of hardware and software in our server network in a timely fashion. In addition, we frequently update our game servers to ensure the stability of our operation and reduce risks.

### ***Competition***

We compete principally with the following three groups of competitors in China:

- online game developers and operators in China, including Tencent Holdings Limited, NetEase.com, Inc., Shanda Games Limited, Perfect World Co., Ltd., Giant Interactive Group Inc., NetDragon Websoft Inc., Kingsoft Corporation Limited, Shenzhen ZQGame Co., Limited, Forgame Holdings Limited, and Taomee Holdings Limited;
- other private companies in China devoted to game development or operation, many of which are backed by venture capital; and
- international competitors.

Our MMOGs currently compete with, among others, the following MMOGs in China:

- Fantasy Westward Journey, developed and operated by NetEase.com, Inc.;
- World of Warcraft, developed by Blizzard Entertainment and operated by NetEase.com, Inc. in China;
- Blade and Soul, developed by Ncsoft Corporation Limited and operated by Tencent Holdings Limited;
- Dungeon and Fighter, Cross Fire and League of Legends developed and operated by Tencent Holdings Limited;
- JX Online III, developed by Kingsoft Corporation Limited; and
- Dota 2, developed by Value Corporation Limited and operated by Perfect World Co., Ltd.

Our Web games currently compete with, among others, the following Web games in China:

- Charmed Westward Journey and Soul Guardian II, developed by Forgame Holdings Limited;
- Jie Ji San Guo, developed by Shanghai Joy You Information Technology Co Limited;
- Lie Yan, developed by Guangzhou Chuangsi Information Technology Limited;
- Tian Shen Zhuan Qi, developed by Beijing Zeus Interactive Technology Limited;
- Qin Beauty, Havoc in Heaven Online, and Battle of the Dragon Kingdoms, developed by the Mokylin Group.

Our game information portal operated through the 17173.com Website currently competes in China with, among others, the following game information portals:

- Duowan.com, operated by YY Inc.; and
- game.qq.com, operated by Tencent Holdings Limited.

Our existing and potential competitors in the online games industry compete with us for talent, game player spending, time spent on game playing, marketing activities, quality of games, and distribution network. Our existing and potential competitors in the online advertising industry compete with us for talent, advertiser spending, number of unique visitors, number of page views, visitors' time spent on Website, and quality of service.

### ***Facilities***

Our principal offices are located in several office buildings in Beijing, Shanghai, Shenzhen, and Fuzhou in China, which comprise an aggregate of approximately 127,197 square meters, including 55,607 square meters of leased properties. Our leases for those leased properties expire between March 2014 and August 2021. We also occupy 3,484 square meters under leases in other countries.

In August 2010, we entered into a contract for the purchase and development of an office building of approximately 56,549 square meters in Beijing to serve as our headquarters, for consideration of approximately \$162.4 million. Under the August 2010 agreement, the purchase price was adjusted based on the actual floor area built, the final unit price agreed to by the parties and cost adjustments, which were agreed to be approximately \$3.2 million, related to changes to the original design of the building. We had paid \$165.2 million to the property developer through December 31, 2013. We occupied the office building in December 2013. The remaining amount will be paid in 2014.





### *Legal Proceedings*

We may be subject to legal proceedings, investigations and claims incidental to the conduct of our business from time to time. We are not currently a party to, nor are we aware of, any legal proceeding, investigation or claim which, in the opinion of our management, is likely to have a material adverse effect on our business, financial condition or results of operations.

### *PRC Regulation*

The following description of PRC regulation is based upon the opinion of Haiwen & Partners, our PRC counsel. For a description of legal risks relating to our ownership structure and business, see “Risk Factors.”

### *Regulatory Authorities*

PRC law, including regulations and interpretations issued by various PRC governmental authorities, covers extensively areas related to the Internet, such as telecommunications, Internet information services, international connections to computer information networks, information security and censorship, that affect our business. PRC governmental authorities which have issued such regulations and interpretations include:

- the State Administration of Press, Publication, Radio, Film and Television, or SAPPRFT, which resulted from the merger of the former General Administration of Press and Publication, or GAPP, with the former State Administration of Radio, Film and Television, or SARFT, in March 2013. The “SAPPRFT” as used in this report refers to the governmental authority that resulted from the merger, as well as to the GAPP and the SARFT separately for periods prior to the merger;
- the Ministry of Culture, or MOC;
- the Ministry of Industry and Information Technology, or MIIT;
- the Ministry of Commerce, or MOFCOM;
- the Ministry of Public Security, or MPS;
- the State Administration of Foreign Exchange, or SAFE;
- the State Administration for Industry and Commerce, or SAIC;
- the State Council Information Office, or SCIO.

### *Regulation of Telecommunication Services*

#### *Regulation of Value-Added Telecommunication Services in General*

The *Telecommunications Regulations of the People’s Republic of China*, or the Telecom Regulations, implemented in September 2000, are the primary PRC regulation governing telecommunications, and set forth the general framework for the provision of telecommunication services by domestic PRC companies. The Telecom Regulations include a requirement that telecommunications service providers procure operating licenses prior to commencing operations. The Telecom Regulations draw a distinction between “basic telecommunications services” and “value-added telecommunications services.” Value-added telecommunications services are defined as telecommunications and information services provided through public networks. The *Catalog of Telecommunications Business*, or the Catalog, was originally issued as an attachment to the Telecom Regulations and updated in 2001 and 2003. The Catalog as updated categorized online data and transaction processing, domestic Internet virtual private networks, Internet data centers, and Internet access search as value-added telecommunications services. Key aspects of our business fall within the definition of value-added telecommunications services under the Telecom Regulations and the Catalog.

The MIIT promulgated the *Administration Measures for Telecommunications Business Operation*, or the Telecom License Measures, in April 2009. The Telecom License Measures include requirements and procedures for obtaining licenses for value-added telecommunications services and provide for a distinction between such a license granted solely for operations within a particular province and such a license granted for “trans-regional” (or multiple-province) activities. Operations under a value-added telecommunications services license must be conducted in accordance with the specific terms of the license. In September 2000, the State Council promulgated the *Administrative Measures on Internet Information Services*, or the Internet Measures. Under the Internet Measures, providers of Internet content services, or ICPs, must obtain a value-added telecommunications license, or ICP license, from governmental authorities before engaging in any commercial ICP operations within the PRC. Each of Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE has obtained an ICP license.



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In 2000, the MIIT promulgated the Internet Electronic Bulletin Service Administrative Measures, or the BBS Measures. The BBS Measures required ICPs to obtain specific approvals before they provided BBS services, which included electronic bulletin boards, electronic forums, message boards and chat rooms. In July 2010, these approval requirements with respect to the operation of BBS services were terminated by a decision issued by the State Council, but in practice certain local authorities still require operating companies to obtain approvals for the operation of BBS services. The ICP licenses held by Gamease and Guanyou Gamespace include such specific approval of the BBS services that they provide. However, although Shenzhen 7Road provides BBS services, its ICP license does not specifically permit the operation of BBS services. It is unclear whether Shenzhen 7Road's provision of BBS services is in violation of applicable regulations. In order to avoid the possibility of being challenged by the relevant local authority for the absence of BBS service approval, Shenzhen 7Road has applied to the Guangdong Communications Administration for amendments of its ICP license to permit or continue to permit its operation of BBS services. Shenzhen 7 Road has been orally informed by the Guangdong Communications Administration that currently there are no specific authorities to approve BBS services in Shenzhen and that new regulations regarding the provision of BBS services may be released in 2014 or 2015. If relevant PRC authorities were to determine that Shenzhen 7Road's provision of BBS services is in violation of the BBS Measures due to the absence of such specific approval, Shenzhen 7Road could be subject to fines up to five times the income it generated from such services and other penalties, including the shutdown of its Websites.

#### *Restrictions on Foreign Ownership of Value-Added Telecommunication Services*

Various PRC regulations currently restrict foreign-invested entities from engaging in value-added telecommunication services, including operating online games and providing Internet information services. Foreign direct investment in telecommunication companies in China is regulated by the *Regulations for the Administration of Foreign-Invested Telecommunications Enterprises*, or the FITE Regulations, issued by the State Council, which became effective in January 2002 and were amended in September 2008. The FITE Regulations stipulate that telecommunications enterprises in the PRC with foreign investors, or FITEs, must be established as Sino-foreign equity joint ventures. Under the FITE Regulations and in accordance with WTO-related agreements, FITEs may provide value-added telecommunications services, but the foreign party to a FITE engaging in such services may hold no more than 50% of the equity of the FITE. The FITE Regulations do not impose geographical restrictions on the operations of a FITE. The PRC government has not made any commitment to liberalize its regulation of the operations of FITEs' providing value-added telecommunications services.

For a FITE to acquire any equity interest in a value-added telecommunications business in China, it must satisfy a number of stringent performance and operational experience requirements, including demonstrating a track record and experience in operating a value-added telecommunications business overseas. Moreover, FITEs that meet these requirements must obtain approvals from the MIIT and the MOFCOM or their authorized local counterparts, which retain considerable discretion in granting approvals.

In July 2006, the MIIT released a *Notice on Strengthening the Administration of Foreign Investment in Operating Value-added Telecommunications Business*, or the MIIT Notice, which reiterates certain provisions under the FITE Regulations. Under the MIIT Notice, if a FITE intends to invest in a PRC value-added telecommunications business, the FITE must be established and must apply for telecommunications business license applicable to its business. Under the MIIT Notice, a domestic company that holds a license for the provision of Internet content services, or an ICP license, as a type of value-added telecommunications business in China, is prohibited from leasing, transferring or selling the license to foreign investors in any form, and from providing any assistance, including providing resources, sites or facilities, to foreign investors to conduct value-added telecommunications businesses illegally in China. Trademarks and domain names that are used in the provision of Internet content services must be owned by the ICP license holder. The MIIT Notice requires each ICP license holder to have appropriate facilities for its approved business operations and to maintain such facilities in the regions covered by its license. In addition, all value-added telecommunications service providers are required to maintain network and information security in accordance with the standards set forth under relevant PRC regulations. Our VIEs, rather than our subsidiaries hold ICP licenses, own our domain names, and hold or have applied for registration in the PRC of trademarks related to our games and the 17173 Business and own and maintain facilities that we believe are appropriate for our business operations.

In view of the restrictions on foreign direct investment in the telecommunications sector, we established or acquired our VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE to engage in value-added telecommunications services. For a detailed discussion of our VIEs, please refer to "Organizational Structure" in Item 4. Due to a lack of interpretative materials from the relevant PRC authorities, there are uncertainties regarding whether PRC authorities would consider our corporate structure and contractual arrangements to be a kind of foreign ownership of value-added telecommunications services. See "Risk Factors—Risks Related to Our Corporate Structure and PRC Law and Regulations—If the PRC government determines that the VIE structure for operating our business does not comply with applicable PRC government restrictions on foreign investment in the online game industry and the online advertisement industry, we could face severe penalties."



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On October 1, 2004, the *Administrative Rules on the Filing of Commercial Websites*, or the Websites Rules, were promulgated by the Beijing Administration of Industry and Commerce, or the Beijing AIC, to replace the *Detailed Implementing Rules for the Measures for the Administration of Commercial website Filings for the Record* promulgated by the Beijing AIC on September 1, 2000. The Websites Rules state that operators of Websites must comply with the following requirements:

- file with the Beijing AIC and obtain electronic registration marks for the Websites;
- place the registration marks on the Websites' homepages; and
- register the Website names with the Beijing AIC.

We have registered our Websites [www.changyou.com](http://www.changyou.com) and [www.cy.com](http://www.cy.com) with the Beijing AIC and an electronic registration mark for the Website is prominently placed on the homepage of the Websites.

#### *Online Games and Cultural Products*

In September 2009, the SAPPRFT, together with the National Copyright Administration, and the National Office of Combating Pornography and Illegal Publications jointly issued a *Notice on Further Strengthening on the Administration of Pre-examination and Approval of Online Game and the Examination and Approval of Imported Online Game*, or the SAPPRFT Online Game Notice. The SAPPRFT Online Game Notice states that foreign investors are not permitted to invest in online game operating businesses in China via wholly foreign-owned entities, China-foreign equity joint ventures or cooperative joint ventures or to exercise control over or participate in the operation of domestic online game businesses through indirect means, such as other joint venture companies or contractual or technical arrangements. If our VIE structure were deemed under the SAPPRFT Online Game Notice to be an "indirect means" for foreign investors to exercise control over or participate in the operation of a domestic online game business, our VIE structure might be challenged by the SAPPRFT. We are not aware of any online game companies which use the same or similar VIE contractual arrangements as those we use having been challenged by the SAPPRFT as using those VIE arrangements as an "indirect means" for foreign investors to exercise control over or participate in the operation of a domestic online game business or having been penalized or ordered to terminate operations since the SAPPRFT Online Game Notice first became effective, but it is unclear whether and how the SAPPRFT Online Game Notice might be interpreted or implemented in the future.

On February 21, 2008, the SAPPRFT issued the Rules for the Administration of Electronic Publications, or the Electronic Publication Rules, which regulate the production, publishing and importation of electronic publications in the PRC and outline a licensing system for business operations involving electronic publishing. Under the Electronic Publication Rules and other related regulations issued by the SAPPRFT, online games are classified as a type of electronic publication or Internet publication that may only be provided by a licensed electronic publishing entity with a standard publication code, and the establishment of an electronic publishing entity must be approved by the SAPPRFT. Electronic publishing entities are responsible for assuring that the content of electronic publications comply with relevant PRC law and regulations, and must obtain the approval of the SAPPRFT before publishing foreign electronic publications. The Tentative Measures for Internet Publication Administration, or the Internet Publication Measures, which were jointly promulgated by the SAPPRFT and the MIIT and became effective in 2002, impose a license requirement for any company that intends to engage in Internet publishing, which is defined as any act by an ICP to select, edit and process content or programs and to make such content or programs publicly available on the Internet. As the provision of online games is deemed to be an Internet publication activity, an online game operator must obtain an Internet publishing license and a publishing number for each of its games in operation in order to directly make those games publicly available in the PRC. Although the Internet Publication Measures do not specifically authorize such a practice, an online game operator is generally able to publish its games and obtain publishing numbers for those games through third-party licensed electronic publishing entities and register the games with the SAPPRFT as electronic publications.

Gamease, which is the operator of TLBB, BO, BH2 and certain other licensed MMOGs, Shenzhen 7Road, which is the operator of DDTank, Wartune and certain other games developed by 7Road, and Guanyou Gamespace, which is the operator of DMD, obtained Internet publishing licenses on December 10, 2010, September 2, 2011, and October 13, 2011, respectively. Shanghai ICE, which is the operator of Tao Yuan, is in the process of applying for an Internet publishing license. TLBB, BO, BH2, DDTank, Wartune and some of our other games were historically published through third parties that were licensed electronic publishing entities, because Gamease, Shenzhen 7Road and Shanghai ICE had not obtained Internet publishing licenses at the time those online games were made publicly available. TLBB, BO and BH2 and certain of our other existing games are currently published under an Internet publishing license held by Gamease and Shenzhen 7Road currently publishes Wartune, DDTank and certain other games developed by 7Road under publishing numbers obtained through Shenzhen 7Road's Internet publishing license. Shanghai ICE continues to publish Tao Yuan with publishing numbers obtained through third-party licensed electronic publishing entities, and Shenzhen 7Road intends to publish certain of its pipeline and future games with publishing numbers obtained through third parties. Current PRC regulations are not clear as to the consequence of obtaining publishing numbers through third-party electronic publishing entities. While we believe that arrangements like ours are acknowledged by the SAPPRFT, in view of the lack of formal interpretation regarding this issue, the SAPPRFT might challenge our current and past practices and could subject us to various penalties, including fines, confiscation of publishing equipment and the revenues generated from the publishing activities, the revocation of our business license, or the forced discontinuation of or restrictions on our operations.



The MOC issued the *New Provisional Regulations for the Administration of Online Culture*, or the Online Culture Regulations, which took effect on April 1, 2011 and replaced the *Provisional Regulations for the Administration of Online Culture*. The Online Culture Regulations apply to entities engaging in activities related to “Internet cultural products,” which include cultural products that are produced specifically for Internet use, such as online music and entertainment, online games, online plays, online performances, online works of art and Web animation, and other online cultural products that through technical means, produce or reproduce music, entertainment, games, plays and other art works for Internet dissemination. Under the New Online Culture Regulations, commercial entities are required to apply to the relevant local branch of the MOC for an Online Culture Operating Permit if they engage in the production, duplication, importation, release or broadcasting of Internet cultural products; the dissemination of online cultural products on the Internet or the transmission of such products via Internet or mobile phone networks to user terminals, such as computers, phones, television sets and gaming consoles, or Internet surfing service sites such as Internet cafés; or the holding or exhibition of contests related to Internet cultural products. In January 2008, Gamease obtained an Online Culture Operating Permit, which was re-certified in August 2013; in June 2010, Shenzhen 7Road obtained an Online Culture Operating Permit, which was re-certified in August 2013; Guanyou Gamespace obtained an Online Culture Operating Permit in June 2011, which was re-certified in July 2013; and Shanghai ICE obtained an Online Culture Operating Permit in December 2010, which was re-certified in January 2014.

The *Interim Measures for the Administration of Online Games*, or the Online Game Measures, issued by the MOC, which took effect on August 1, 2010, regulate a broad range of activities related to the online games business, including the development, production and operation of online games, the issuance of virtual currencies used for online games, and the provision of virtual currency trading services. The Online Game Measures provide that any entity that is engaged in online game operations must obtain an Online Culture Operating Permit, and require the content of an imported online game to be examined and approved by the MOC prior to the game’s launch and a domestic online game to be filed with the MOC within 30 days after its launch. The *Notice of the Ministry of Culture on the Implementation of the Interim Measures for the Administration of Online Games*, which was issued by the MOC on July 29, 2010 to implement the Online Game Measures (i) requires online game operators to protect the interests of online game users and specify certain terms that must be included in service agreements between online game operators and the users of their online games, (ii) specifies content review of imported online games and filing procedures for domestic online games, (iii) emphasizes the protection of minors playing online games and (iv) requests online game operators to promote real-name registration by their game users. We filed our games TLBB, DDTank, Wartune, BO, BH2, DMD, DSH, DPCQ and certain of our other existing games with the MOC. If we fail to maintain any of our permits, approvals or registrations, to make any necessary filings, or to apply for and obtain any required new permits, approvals or registrations or make any new filings on a timely basis, we may be subject to various penalties, including fines and a requirement that we discontinue or limit our operations.

The *Notice on Strengthening the Approval and Administration of Imported Online Games*, or the SAPPRFT Imported Online Game Notice, which was issued by the SAPPRFT and took effect in July 2009, states that the SAPPRFT is the only governmental department authorized by the State Council to approve the importation of online games from offshore copyright owners, and that any enterprise which engages in online game publication and operation services within China must have the game examined and approved by the SAPPRFT and receive from the SAPPRFT an Internet publishing license. Our VIEs Gamease, Shenzhen 7Road and Guanyou Gamespace have obtained Internet publishing licenses from the SAPPRFT. In addition, the SAPPRFT Imported Online Game Notice states that activities which involve the showing, exhibition, trading and promotion of offshore online games in China also must be examined and approved by the SAPPRFT.

The *Notice Regarding Improving and Strengthening the Administration of Online Game Content*, or the Online Game Content Notice, issued by the MOC in November 2009, calls for online game operators to improve and adapt their game models by (i) mitigating the predominance of the “upgrade by monster fighting” model, (ii) limiting the use of the “player kill” model (where one player’s character attempts to kill another player’s character), (iii) limiting in-game marriages among game players, and (iv) improving their compliance with legal requirements for the registration of minors and game time-limits.

The *Administrative Measures for Content Self-review by Internet Culture Business Entities*, or the Content Self-review Administrative Measure, which took effect in December 2013, require Internet culture business entities to review the content of products and services to be provided prior to providing such content and services to the public. The content management system of an Internet culture business entity is required to specify the responsibilities, standards and processes for content review as well as accountability measures, and is required be filed with the local provincial branch of the MOC.

The *Interim Measures for the Administration of Online Commodities Trading and Relevant Services*, or the Online Commodities Trading Measures, issued by the SAIC, which took effect on July 1, 2010, regulate online commodity trading and online service activities. The Online Commodities Trading Measures require that online service providers ensure that information which they release online is accurate and complete and comply with all applicable laws with respect to the protection of intellectual property rights of others and the prevention of unfair competition. If we fail to comply with all requirements of such regulations, the local branch of the SAIC may suggest that the relevant local telecommunication authorities shut down our Websites.





### Online Audiovisual Transmission

The SAPPRFT issued the *Measures for the Administration of the Transmission of Audiovisual Programs over Internet and other Information Networks*, which were effective in October, 2004. Under these measures, Websites engaging in the business of network audiovisual program dissemination are required to obtain a Permit for the Network Transmission of Audiovisual Programs from the SAPPRFT.

The SAPPRFT and the MIIT jointly issued the *Rules for the Administration of Internet Audiovisual Program Services*, or Document 56, which went into effect in January 2008. Under Document 56, all online audio and video service providers must be either state-owned or state-controlled. However, at a press conference held on February 3, 2008, the SAPPRFT and the MIIT clarified that online audio-visual service providers that had been lawfully conducting the business prior to the issuance of Document 56 may re-register and continue to operate without becoming state-owned or controlled, provided that such providers do not engage in any unlawful activities. This exemption will not be granted to service providers set up after the issuance of Document 56.

### Advertisings Services

Under the *Administrative Regulations for Advertising Licenses* and the *Implementation Rules for the Administrative Regulations for Advertising*, issued by the State AIC and effective in January, 2005, broadcast stations, television stations, newspapers and magazines, non-corporate entities and other specified entities are required to obtain a license that is specifically for their advertising services. Other enterprises are only required to include advertising services within their overall business licenses. Both of Guanyou Gamespace, which is the operator of our online advertisement business, and Shanghai Jingmao, which primarily engages in the cinema advertising business, have included advertising services in their respective business licenses.

### Registration of Software Products

The *Measures Concerning Software Products Administration*, or the Software Measures, issued by the MIIT, which became effective in April 2009 and replaced measures which had been in effect since 2000, permit software developers and producers to sell or license their software products independently or through agents, and software products developed in the PRC can be registered with the local provincial government authorities in charge of the information industry and filed with the MIIT. Upon registration, the software products are granted registration certificates which are valid for five years and may be renewed upon expiration. Under policies promulgated by the State Council, software products developed in the PRC which satisfy the requirements of the Software Measures and have been registered and filed in accordance with the Software Measures may enjoy certain types of preferential treatment. State Council policies provide that the MIIT and other relevant departments may supervise and inspect the development, production, sale, import and export of software products in the PRC. We have registered software copyrights covering all of our significant copyrightable products and enhancements.

### Import and Export of Software Technology

China imposes controls on the import and export of technology and software products. Under the *Regulations on Administration of Import and Export of Technologies* promulgated by the State Council, the term “technology import and export” is defined to include, among other things, the transfer or licensing of patents and know-how, and the provision of services related to technology. Depending on the nature of the relevant technology, the import and export of technology require either approval by or registration with the relevant PRC governmental authorities. Under the *Software Export Management and Statistics Measures* promulgated in October 2001, if a company is classified as a software enterprise and has a minimum of RMB1 million in registered capital, it may engage in an export business after being registered with the relevant PRC governmental authorities. All contracts which relate to the export of software products, transfer of technology and provision of related services must be filed with the relevant PRC governmental authorities. The *Measures for the Administration of Registration of Technology Import and Export Contracts*, issued by the MOFCOM in February 2009, specify registration requirements related to the import and export of technology.

We have entered into license agreements with third parties outside of China to license our games, which may be deemed to constitute the export of technology under the regulations. As a result, such licenses are required to be registered with applicable PRC governmental authorities. Although there are no explicit penalties set forth in these regulations for lack of such registration, failure to register an agreement where such registration is required may result in restrictions concerning foreign exchange, banking and taxation matters relating to such agreements. We have not registered all of the game license agreements under which we authorize overseas third-party online game operators to operate our online games, and so far we have not encountered any problems with respect to foreign exchange, banking and taxation matters relating to our license agreements, nor have we received any notice from any governmental authority requiring us to complete the registration of our game license agreements.





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*Regulation of Internet Content*

The PRC government has promulgated measures relating to Internet content through a number of government authorities, including but not limited to the MIIT, the MOC, the SAPPRFT and the MPS. These measures specifically prohibit certain Internet activities, including the operation of online games that result in the publication of any content which is found to, among other things, propagate obscenity, gambling or violence, instigate crimes, undermine public morality or the cultural traditions of the PRC, or compromise State security or secrets. If an ICP license holder violates these measures, the PRC government may revoke its ICP license and shut down its Websites.

In addition, the PRC governmental authorities have issued several regulations requiring the installation of software to filter out unhealthy and vulgar content from the Internet. In April 2009, the Ministry of Education, the MIIT and other ministries and agencies issued a notice requiring that, by the end of May 2009, all computer terminals connected with the Internet at all elementary and secondary schools be able to include and operate Green Dam-Youth Escort, which is a software aimed at filtering out unhealthy and vulgar content in text and graphics from the Internet and which, according to the Website for the software, may be used to control time spent on the Internet, prohibit access to computer games, and filter out unhealthy Websites. The MIIT further expanded the scope of required use of this filter software by issuing a notice in May 2009 requiring that, effective as of July 1, 2009, all computers manufactured and sold in China have the latest available version of Green Dam-Youth Escort preinstalled when they leave the factory and that all imported computers have the latest available version of Green Dam-Youth Escort preinstalled before being sold in China. Green-Dam Youth Escort is to be preinstalled on the hard drive of the computer or in the form of a CD accompanying the computer and is also to be included in the backup partition and system restore CD. However, in June 2009, the MIIT announced that it was postponing the implementation of this requirement regarding pre-installation of Green Dam-Youth Escort.

*Information Security and Censorship*

Internet content in China is also regulated and restricted from a State security standpoint. The Standing Committee of National People's Congress enacted the *Decision on Internet Security Protection* in 2000, and amended it in August, 2009. The decision makes it unlawful to: (i) gain improper entry into a computer or system of strategic importance; (ii) disseminate politically disruptive information; (iii) leak State secrets; (iv) spread false commercial information; or (v) infringe intellectual property rights. The Ministry of Public Security has promulgated measures that prohibit the use of the Internet in ways which, among other things, result in a leakage of State secrets or distribution of socially destabilizing content. The Ministry of Public Security has supervision and inspection rights in this regard, and we may be subject to the jurisdiction of the local security bureaus. If an ICP license holder violates these measures, the PRC government may revoke its ICP license and shut down its Websites.

In 2004, the MOC issued a *Notice Regarding the Strengthening of Online Game Censorship*. This notice mandates the establishment of a new committee under the MOC that will screen the content of imported online games. In addition, all imported and domestic online games are required to be filed with the MOC. We have submitted the relevant filing documents to the MOC for the filing of all our games in operation.

In 2005, the MOC and the MIIT promulgated the *Opinions on the Development and Administration of Online Game* emphasizing the PRC government's intent to foster and control the development of the online game industry in China and providing that the MOC will censor online games that "threaten state security," "disturb the social order," or contain "obscenity" or "violence."

In April, 2009, the MOC issued a *Public Announcement on Regulating Applications for the Examination of the Content of Imported Online Game*, or the Announcement. The Announcement emphasizes that enterprises operating imported online games must have the content of those games examined and approved by the MOC.

*Internet Café Regulation*

Internet cafés are required to obtain an Online Culture Operating Permit from the MOC and file the permit with the SAIC, and are subject to requirements and regulations with respect to location, size, number of computers, ages of customers and hours of operation. In 2004, the MOC, the SAIC and some other governmental authorities jointly issued a notice to suspend issuance of new Internet café licenses. Though this nationwide suspension was generally lifted in 2005, local authorities have the authority in their discretion to control the number of new licenses and determine the recipients of new licenses. In addition, local and higher-level governmental authorities may from time to time strictly enforce customer age limits and other requirements relating to Internet cafés, as a result of the occurrence of, and media attention on, gang fights, arson or other incidents in or related to Internet cafés. On February 15, 2007, the MOC and other relevant government authorities jointly issued a *Notice on the Reinforcement of the Administration of Internet Cafés and Online Games*, or the Internet Cafés Notice, which suspended nationwide approval for the establishment of new Internet cafés in 2007 and imposed tougher penalties for Internet cafés admitting minors. In 2008, 2009 and 2010, the MOC, the SAIC and other relevant government authorities, individually or jointly, issued several notices which provide various ways to strengthen the regulation of Internet cafés, including investigating and punishing Internet cafés which accept minors, cracking down on Internet cafés without sufficient and valid licenses, limiting the total number of Internet cafés, screening unlawful games and Websites, and improving the coordination of regulation of Internet cafés and online games. As many of our customers access our games from Internet cafés, any reduction in the number, or any slowdown in the growth, of Internet cafés in China as a result of stricter Internet café regulation will limit our ability to maintain or increase our revenues and expand our customer base.



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*Protection of Minors*

On April 15, 2007, the SAPPRFT and several other governmental authorities issued a circular requiring the implementation of an “anti-fatigue system” and a real-name registration system by all PRC online game operators, in an effort to curb addictive online game play behaviors of minors. Under the anti-fatigue system, three hours or less of continuous play by minors is considered to be “healthy,” three to five hours to be “fatiguing,” and five hours or more to be “unhealthy.” Game operators are required to reduce the value of in-game benefits to a game player by half if the game player has reached “fatiguing” level, and to zero in the case of “unhealthy” level.

To identify whether a game player is a minor and thus subject to the anti-fatigue system, there was adopted a real-name registration system, which requires online game players to register their real identity information before they play online games and requires us to submit the identity information of game players to the public security authorities for verification. On July 1, 2011, the SAPPRFT, the MIIT, the Ministry of Education and five other governmental authorities issued a *Notice on Initializing the verification of Real-name Registration for Anti-Fatigue System on Internet Games*, or the Real-name Registration Notice, to strengthen the implementation of the anti-fatigue system and real-name registration, which took effect on October 1, 2011. The Real-name Registration Notice’s main focus is to prevent minors from using an adult’s ID to play Internet games and, accordingly, the notice imposes stringent punishments on online game operators that do not implement the required anti-fatigue and real-name registration measures properly and effectively. The most severe punishment contemplated by the Real-name Registration Notice is to require termination of the operation of the online game if it is found to be in violation of the Anti-Fatigue Notice, the Monitor System Circular or the Real-name Registration Notice. We developed our own anti-fatigue and real-name registration systems for our games, and implemented them beginning in 2007. Under our system, game players must use real identification in order to create accounts, and in this way, we are able to tell which of our game players are minors and thus subject to these regulations. For game players who do not register, we assume that they are minors. In order to comply with the anti-fatigue rules, game players under 18 years of age only receive half of the experience time they actually earn after three hours of play. And, after five hours of play, minors receive no experience points. We use this system to disincentivize minors from playing in excess of five hours at a time.

On January 15, 2011, the MOC, the MIIT and six other central government authorities jointly issued a circular entitled *Implementation of Online Game Monitor System of the Guardians of Minors*, or the Monitor System Circular, aiming to provide specific protection measures to monitor the online game activities of minors and curb addictive online game playing behaviors of minors. Under the Monitor System Circular, online game operators are required to adopt various measures to maintain a system to communicate with the parents or other guardians of minors playing online games and online game operators are required to monitor the online game activities of minors, and must suspend the account of a minor if so requested by the minor’s parents or guardians. The monitor system was formally implemented commencing March 1, 2011.

In February 2013, 15 PRC government authorities, including the SAPPRFT, the Ministry of Education, the MOC and the MIIT, jointly issued the *Work Plan for the Integrated Prevention of Minors Online Game Addiction*, or the Work Plan, implementing integrated measures by different authorities to prevent minors from being addicted to online games. Under the Work Plan, the current relevant regulations regarding online games will be further clarified and additional implementation rules will be issued; and as a result, online game operators will be required to implement measures to protect minors.

*Virtual Currency*

On February 15, 2007, the MOC, the PBOC and other relevant government authorities jointly issued the Internet Cafés Notice. Under the Internet Cafés Notice, the PBOC is directed to strengthen the administration of virtual currency in online games to avoid any adverse impact on the economy and financial system. The Internet Cafés Notice provides that the total amount of virtual currency issued by online game operators and the amount purchased by individual game players should be strictly limited, with a strict and clear division between virtual transactions and real transactions carried out by way of electronic commerce. This notice also provides that virtual currency should only be used to purchase virtual items.

On June 4, 2009, the MOC and the MOFCOM jointly issued the *Notice on Strengthening the Administration of Online Game Virtual Currency*, or the Virtual Currency Notice, to regulate the trading of online game virtual currencies. The Virtual Currency Notice defines the meaning of virtual currency and places a set of restrictions on the trading and issuance of virtual currency. The Virtual Currency Notice also states that online game operators are not allowed to give out virtual items or virtual currency through lottery-base activities, such as lucky draws, betting or random computer sampling, etc., in exchange for user’s cash or virtual money. The Virtual Currency Notice is mainly targeted at lottery-based activities relating to “treasure box” found in some online games.

On July 20, 2009, the MOC promulgated the *Filing Guidelines on Online Game Virtual Currency Issuing Enterprise and Online Game Virtual Currency Trading Enterprise*, which specifically defines the meanings of “issuing enterprise” and “trading enterprise” and stipulates that both of these businesses may not be operated by the same enterprise.



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*Internet Privacy*

The PRC Constitution states that PRC law protects the freedom and privacy of the communications of citizens and prohibits infringement of such rights. In recent years, PRC government authorities have issued various regulations on the use of the Internet that are designed to protect personal information from unauthorized disclosure. For example, the Internet Measures prohibit an Internet information services provider from insulting or slandering a third party or infringing upon the lawful rights and interests of a third party. Under the BBS Measures, ICPs that provide electronic messaging services must not disclose any user's personal information to any third party without such user's consent, unless the disclosure is required by PRC law. ICPs are subject to legal liability if unauthorized disclosure causes damages or losses to users. In addition, PRC regulations authorize PRC telecommunication authorities to demand rectification of unauthorized disclosure by ICPs.

PRC law does not prohibit Internet content providers from collecting and analyzing personal information from their users. The PRC government, however, has the power and authority to order ICPs to submit personal information of an Internet user if such user posts any prohibited content or engages in illegal activities on the Internet. In addition, the MIIT promulgated the *Several Provisions on Regulating the Market Order of Internet Information Services*, which became effective as of March 15, 2012. This regulation stipulates that ICPs must not, without users' consent, collect information on users that can be used, alone or in combination with other information, to identify the user, or User Personal Information, and may not provide any User Personal Information to third parties without prior user consent. ICPs may only collect User Personal Information necessary to provide their services and must expressly inform the users of the method, content and purpose of the collection and processing of such User Personal Information. In addition, an ICP may use User Personal Information only for the stated purposes under the ICP's scope of services. ICPs are also required to ensure the proper security of User Personal Information, and take immediate remedial measures if User Personal Information is suspected to have been disclosed. If the consequences of any such disclosure are expected to be serious, the ICP must immediately report the incident to the telecommunications regulatory authorities and cooperate with the authorities in their investigations. In addition, the PRC government has the power and authority to order ICPs to submit personal information of an Internet user if such user posts any prohibited content or engages in any illegal activity on the Internet. We require our users to accept a user agreement whereby they agree to provide certain personal information to us. If we violate these regulations, the MIIT or its local bureaus may impose penalties and we may be liable for damages caused to our users.

On December 28, 2012, the Standing Committee of the National People's Congress enacted the *Decision to Enhance the Protection of Network Information*, or the Information Protection Decision, to further enhance the protection of User Personal Information in electronic form. The Information Protection Decision provides that ICPs must expressly inform their users of the purpose, manner and scope of the ICPs' collection and use of User Personal Information, publish the ICPs' standards for their collection and use of User Personal Information, and collect and use User Personal Information only with the consent of the users and only within the scope of such consent. The Information Protection Decision also mandates that ICPs and their employees must keep strictly confidential User Personal Information that they collect, and that ICPs must take such technical and other measures as are necessary to safeguard the information against disclosure.

On July 16, 2013, the MIIT issued the Order for the Protection of Telecommunication and Internet User Personal Information or the Order. Most requirements under the Order that are relevant to ICP operators are consistent with the requirements already established under the MIIT provisions as discussed elsewhere in this annual report. Under the Order, these requirements are often stricter and have a wider scope. If an ICP operator wishes to collect or use personal information, it may do so only if such collection is necessary for the services it provides. Further, the operator must disclose to its users the purpose, method and scope of any such collection or use, and must obtain consent from its users whose information is being collected or used. ICP operators are also required to establish and publish their rules relating to personal information collection or use, keep any collected information strictly confidential, and take technological and other measures to maintain the security of such information. ICP operators are required to cease any collection or use of the user personal information, and de-register the relevant user account, when a given user stops using the relevant Internet service. ICP operators are further prohibited from divulging, distorting or destroying any such personal information, or selling or providing such information unlawfully to other parties. In addition, if an ICP operator appoints an agent to undertake any marketing or technical services that involve the collection or use of personal information, the ICP operator is still required to supervise and manage the protection of the information. As to penalties, in very broad terms, the Order states that violators may face warnings, fines, and disclosure to the public and, in severe cases, criminal liability.

Our current security measures and those of the third parties with whom we transact business may not be adequate for the protection of User Personal Information. In addition, we do not have control over the security measures of our third-party online payment vendors. Security breaches of our system and the online payment systems that we use could expose us to litigation and liability for failing to secure confidential customer information and could harm our reputation, ability to attract customers and ability to encourage customers to purchase virtual items.

*Regulation of Copyright Protection*

The *PRC Copyright Law*, which was adopted by the Standing Committee of the National People's Congress in 1990 and subsequently amended in 2001 and 2010, extends copyright protection to Internet activities, products disseminated over the Internet and software products. In addition, there is a voluntary registration system administered by the China Copyright Protection Center.

*The Rules of Protection on Information Network Dissemination Rights*, promulgated by the State Council in May 2006 and amended in January 2013, address copyright issues relating to the Internet. In addition, on December 17, 2012, the Supreme People's Court promulgated *the Provisions on Several Issues Concerning the Application of Law for Trial of Civil Dispute Cases Involving Infringement of the Right to Network Dissemination of Information*, which stipulate that the dissemination by network users or network service providers of works, performance or audio or video recordings without the permission of the holder of the rights to such dissemination will constitute infringement of such rights, and that network service providers that aid or abet any network user's infringement of the rights of another to network dissemination of any works or recordings may be liable for such network user's infringing activities.

*Employment Contracts*

On June 29, 2007, the National People's Congress promulgated the *Employment Contract Law of PRC*, or ECL, which became effective as of January 1, 2008, and was amended on December 28, 2012. The ECL requires employers to provide written contracts to their employees, restricts the use of temporary workers and aims to give employees long-term job security.

Pursuant to the ECL, employment contracts lawfully concluded prior to the implementation of the ECL and continuing as of the date of its implementation shall continue to be performed. Where an employment relationship was established prior to the implementation of the ECL but no written employment contract was concluded, a contract must be concluded within one month after its implementation.

Our standard employment contract complies with the requirements of the ECL and its implementing regulations.

*Regulation of Foreign Currency Exchange and Dividend Distribution*

**Foreign Currency Exchange.** The principal regulations governing foreign currency exchange in China are the Foreign Exchange Administration Regulations, as amended in August 2008. Under the *Foreign Exchange Administration Regulations*, the RMB is freely convertible for current account items, including the distribution of dividends, interest payments, trade and service-related foreign exchange transactions, but not for capital account items, such as direct investments, loans, repatriation of investments and investments in securities outside of China, unless the prior approval of the SAFE is obtained and prior registration with the SAFE is made. On August 29, 2008, the SAFE promulgated a notice, Circular 142, regulating the conversion by a foreign-invested company of foreign currency into RMB by restricting how the converted RMB may be used. The notice requires that the registered capital of a foreign-invested company settled in RMB converted from foreign currencies may only be used for purposes within the business scope approved by the applicable governmental authority and may not be used for equity investments within the PRC. In addition, the SAFE strengthened its oversight of the flow and use of the registered capital of a foreign-invested company settled in RMB converted from foreign currencies. The use of such RMB capital may not be changed without the 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 will result in severe penalties, such as heavy fines. As a result, Circular 142 may significantly limit our ability to transfer the net proceeds from our initial public offering to Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE through our subsidiaries in the PRC, which may adversely affect the business expansion of Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, and we may not be able to convert the net proceeds into RMB to invest in or acquire any other PRC companies, or establish other VIEs in the PRC.

Dividends paid by a subsidiary to its overseas shareholder are deemed income of the shareholder and are taxable in China. Pursuant to the *Administration Rules of the Settlement, Sale and Payment of Foreign Exchange* (1996), foreign-invested enterprises in China may purchase or remit foreign currency, subject to a cap approved by the SAFE, for settlement of current account transactions without the approval of the SAFE. Foreign currency transactions under the capital account are still subject to limitations and require approvals from, or registration with, the SAFE and other relevant PRC governmental authorities.





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**Circular 75.** On October 21, 2005, the SAFE issued Circular 75, which became effective as of November 1, 2005. Under Circular 75, prior registration with the local SAFE branch is required for PRC residents to establish or to control an offshore company for the purposes of financing that offshore company with assets or equity interests in an onshore enterprise located in the PRC. An amendment to registration or filing with the local SAFE branch by such PRC resident is also required for the injection of equity interests or assets of an onshore enterprise in the offshore company or overseas funds raised by such offshore company, or any other material change involving a change in the capital of the offshore company. Moreover, Circular 75 applies retroactively. As a result, PRC residents who have established or acquired control of offshore companies that have made onshore investments in the PRC in the past are required to complete the relevant registration procedures with the local SAFE branch by March 31, 2006. Since May 2007, the SAFE has issued guidance to its local branches from time to time with respect to the procedures for SAFE registration under Circular 75. The guidance specified stringent procedures for complying with the registration requirements of Circular 75. For example, the guidance imposes obligations on an onshore subsidiary of an offshore entity to provide to the local SAFE authorities detailed and accurate information regarding any shareholder or beneficial owner of the offshore entity who is a PRC citizen or resident. Untrue statements by the onshore subsidiaries will lead to potential liability for the subsidiaries, and in some instances, for their legal representatives and other individuals affiliated with the subsidiaries. Under the relevant rules, failure to comply with the registration procedures set forth in Circular 75 may result in restrictions being imposed on the foreign exchange activities of the relevant onshore company, including the increase of its registered capital, the payment of dividends and other distributions to its offshore parent or affiliate and the capital inflow from the offshore entity, and may also subject relevant PRC residents to penalties under PRC foreign exchange administration regulations. PRC residents who control our company from time to time are required to register with the SAFE in connection with their investments in us. See “Risk Factors—Regulations relating to offshore investment activities by PRC residents may limit our ability to acquire PRC companies and could adversely affect our business.”

**Share Option Rules.** On December 25, 2006, the PBOC issued the *Administration Measures on Individual Foreign Exchange Control*, and its Implementation Rules was issued by SAFE on January 5, 2007, both of which became effective on February 1, 2007. Under these regulations, all foreign exchange transactions involving in an employee share incentive plan, share option plan or similar plan participated in by onshore individuals may be conducted only with the approval from the SAFE or its authorized branch. Under the *Notice of Issues Related to the Foreign Exchange Administration for Domestic Individuals Participating in Stock Incentive Plan of Overseas Listed Company*, or the Offshore Share Incentives Rules, which was issued by the SAFE on February 15, 2012, PRC citizens who are granted share options, restricted share units or restricted shares by an overseas publicly listed company are required to register with the SAFE or its authorized branch and to comply with a series of other requirements. On February 21, 2012, the SAFE approved our application to designate our PRC subsidiary AmazGame to handle registrations and other procedures required by the Offshore Share Incentives Rules. If we and our PRC employees who hold options, restricted share units or restricted shares fail to comply with these registration or other procedural requirements, we and such employees may be subject to fines and other legal sanctions.

**Dividend Distribution.** The principal regulations governing distribution of dividends of foreign holding companies include the *Foreign Investment Enterprise Law* (1986), as amended in October 2000, and the *Administrative Rules under the Foreign Investment Enterprise Law* (1990), as amended in April 2001.

Under these regulations, foreign investment enterprises in China may pay dividends only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. In addition, foreign investment enterprises in China are required to allocate at least 10% of their respective accumulated profits each year, if any, to fund certain reserve funds unless these reserves have reached 50% of the registered capital of the enterprises. These reserves are not distributable as cash dividends. Under the CIT Law, effective January 1, 2008, the maximum tax rate for the withholding tax imposed on dividend payments from PRC foreign invested companies to their overseas investors that are not regarded as “resident” for tax purposes is 10%. The rate is reduced to 5% under tax treaties and arrangements between the PRC and certain other countries and administrative regions.

### *M&A Regulations and Overseas Listings*

On August 8, 2006, six PRC regulatory agencies, consisting of the MOC, the State Assets Supervision and Administration Commission, the SAT, the SAIC, the CSRC, and the SAFE, jointly issued the M&A Rules, which became effective on September 8, 2006 and were amended on June 22, 2009. The M&A Rules, among other things, includes provisions that purport to require that an offshore special purpose vehicle formed for purposes of overseas listing of equity interests in PRC companies and controlled directly or indirectly by PRC companies or individuals obtain the approval of the CSRC prior to the listing and trading of such special purpose vehicle’s securities on an overseas stock exchange.





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On September 21, 2006, the CSRC published on its official Website procedures regarding its approval of overseas listings by special purpose vehicles. The CSRC approval procedures require the filing of a number of documents with the CSRC. The application of this new PRC regulation remains unclear, with no consensus currently existing among leading PRC law firms regarding the scope of the applicability of the CSRC approval requirement.

The M&A Rules also establish procedures and requirements that could make some acquisitions of Chinese companies by foreign investors more time-consuming and complex, including requirements in some instances that the MOFCOM be notified in advance of any change-of-control transaction in which a foreign investor takes control of a Chinese domestic enterprise.

In February 2011, the General Office of the State Council promulgated a *Notice on Establishing the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors*, or Circular 6, which established a security review system for mergers and acquisitions of domestic enterprises by foreign investors. Under Circular 6, a security review is required for mergers and acquisitions by foreign investors having “national defense and security” concerns and mergers and acquisitions by which foreign investors may acquire the “de facto control” of domestic enterprises with “national security” concerns. In August 2011, the MOFCOM promulgated the *Rules on Implementation of Security Review System*, or the MOFCOM Security Review Rules, to replace the *Interim Provisions of the Ministry of Commerce on Matters Relating to the Implementation of the Security Review System Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* promulgated by the MOFCOM in March 2011. The MOFCOM Security Review Rules, which came into effect on September 1, 2011, provide that the MOFCOM will look into the substance and actual impact of a transaction and prohibit foreign investors from bypassing the security review requirement by structuring transactions through proxies, trusts, indirect investments, leases, loans, control through contractual arrangements or offshore transactions.

### Organizational Structure

Changyou.com Limited is an indirect subsidiary of Sohu.com Inc. (NASDAQ: SOHU). As of February 21, 2014, Sohu indirectly held approximately 67.9% of the combined total of Changyou’s outstanding Class A and Class B ordinary shares and controlled approximately 83.0% of the total voting power in Changyou.

As of the date of this annual report, we operate our business through the following wholly-owned subsidiaries:

- Changyou.com (HK) Limited, or Changyou HK, incorporated in Hong Kong on August 13, 2007 as a direct wholly-owned subsidiary of Changyou. Changyou HK is our intermediate offshore holding company for our operations in China and overseas.
- ICE Entertainment (HK) Limited, or ICE HK, incorporated in Hong Kong on July 17, 2007 and acquired by us in May 2010 as a direct wholly-owned subsidiary of Changyou HK.
- Beijing AmazGame Age Internet Technology Co., Ltd., or AmazGame, incorporated in the PRC on September 26, 2007 as a WFOE and a direct wholly-owned subsidiary of Changyou HK.
- Beijing Changyou Gamespace Software Technology Co., Ltd., or Gamespace, incorporated in the PRC on October 29, 2009 as a WFOE and a direct wholly-owned subsidiary of Changyou HK.
- ICE Information Technology (Shanghai) Co., Ltd, or ICE Information, incorporated in the PRC on August 29, 2007 as a WFOE and acquired by us in May 2010 as a direct wholly-owned subsidiary of ICE HK.
- Beijing Yang Fan Jing He Information Consulting Co., Ltd, or Yang Fan Jing He, incorporated in the PRC on April 22, 2010 as a direct wholly-owned subsidiary of AmazGame.
- Shanghai Jingmao Culture Communication Co., Ltd, or Shanghai Jingmao, incorporated in the PRC on April 30, 2009 and acquired by us in January 2011 as a direct wholly-owned subsidiary of Yang Fan Jing He.
- Beijing Changyou Jingmao Film & Culture Communication Co., Ltd., or Beijing Jingmao, incorporated in the PRC on November 16, 2010 and a direct wholly-owned subsidiary of Yang Fan Jing He.
- Shanghai Hejin Data Consulting Co., Ltd, or Shanghai Hejin, incorporated in the PRC on December 2, 2008 and acquired by us in January 2011 as a direct wholly-owned subsidiary of Yang Fan Jing He.
- Changyou.com (US) LLC, or Changyou US, incorporated in the United States on January 26, 2009, as a direct wholly-owned subsidiary of Gamestar HK.
- Changyou.com (UK) Co., Ltd., or Changyou UK, incorporated in the United Kingdom on July 3, 2009, as a direct wholly-owned subsidiary of Changyou HK.



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**CHANGYOU.COM LIMITED**

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- Changyou My Sdn. Bhd, or Changyou Malaysia, incorporated in Malaysia on September 10, 2009, as a direct wholly-owned subsidiary of Changyou HK.
- Changyou.com Korea Limited, or Changyou Korea, incorporated in South Korea on January 7, 2010, as a direct wholly-owned subsidiary of Changyou HK.
- Changyou.com India Private Limited, or Changyou India, incorporated in India on March 11, 2011 as a direct subsidiary of Changyou HK and Changyou UK.
- Changyou.com Gamepower (HK) Limited, or Gamepower HK, incorporated in Hong Kong on September 8, 2011 as a direct wholly-owned subsidiary of Changyou HK.
- Changyou.com Webgames (HK) Limited, or Webgames HK, incorporated in Hong Kong on September 21, 2011 and a direct wholly-owned subsidiary of Changyou HK.
- 7Road.com Limited, or 7Road Cayman, incorporated in the Cayman Islands on June 15, 2011 and a direct wholly-owned subsidiary of Webgames HK.
- 7Road.com HK Limited, or 7Road HK, incorporated in Hong Kong in July 2011 as a direct wholly-owned subsidiary of 7Road Cayman.
- Shenzhen 7Road Network Technologies Co., Ltd., or 7Road Technology, incorporated in the PRC on December 1, 2011 as a wholly-owned subsidiary of 7Road HK.
- CHANGYOU BİLİŞİM HİZMETLERİ TİCARET LİMİTED ŞİRKETİ, or Changyou Turkey, incorporated in Turkey on September 29, 2011 as a direct subsidiary of Changyou HK and Changyou UK.
- Kylie Enterprises Limited, or Kylie, incorporated in British Virgin Islands on October 30, 2003 and acquired by us in December 2011 as a direct wholly-owned subsidiary of Changyou HK.
- Changyou.com Gamestar (HK) Limited, or Gamestar HK, incorporated in Hong Kong on July 12, 2013, as a direct wholly-owned subsidiary of Changyou HK.
- Heroic Vision Holdings Limited, or Heroic, incorporated in the British Virgin Islands on October 23, 2013 as a direct wholly-owned subsidiary of Changyou HK
- Mobogarden Enterprises Limited, or Mobogarden, incorporated in British Virgin Islands on September 25, 2013 as a direct wholly-owned subsidiary of Kylie.

As of the date of this annual report, we also, operate our business through the following majority-owned subsidiaries:

- TalkTalk Limited, or TalkTalk, incorporated in the British Virgin Islands, a majority of which was acquired on December 24, 2013 by Heroic.
- RaidCall (HK) Limited, or RaidCall HK, a Hong Kong company which is a wholly-owned subsidiary of TalkTalk.
- Beijing Changyou RaidCall Internet Technology Co., Ltd., or Changyou RaidCall, a PRC company which is a wholly-owned subsidiary of RaidCall HK.

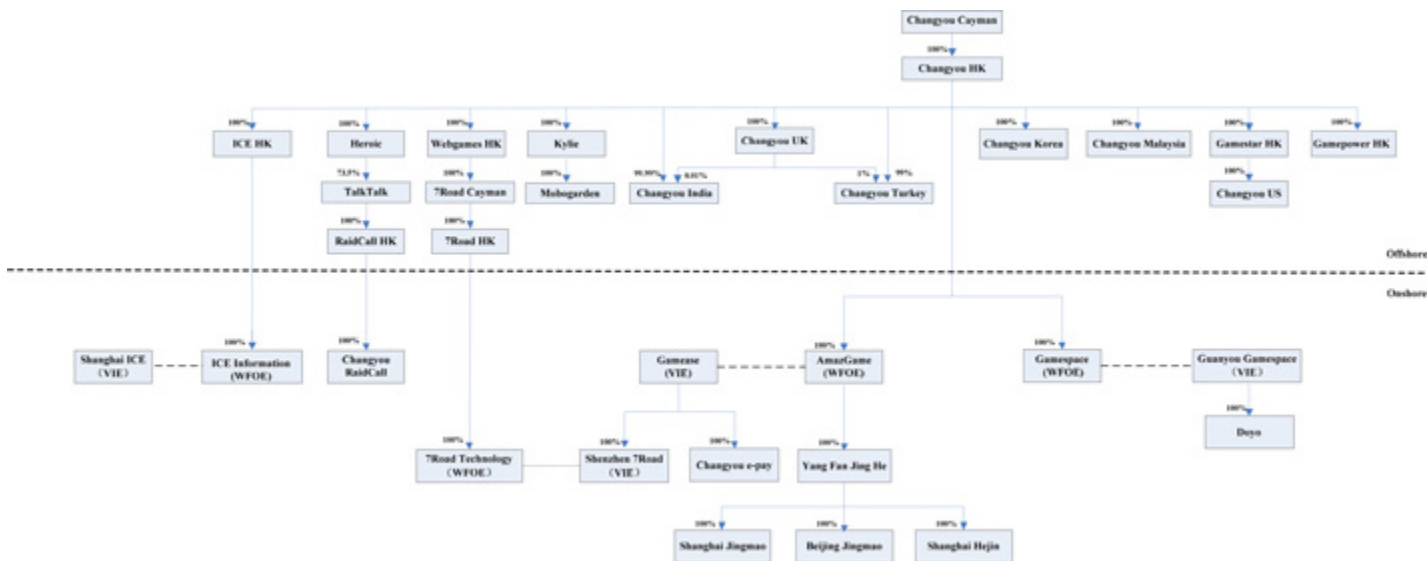
In order to comply with PRC law restricting foreign ownership in the online game business in China, we conduct the operations of our online game business and our online advertising business in China through our VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE rather than through our subsidiaries, and substantially all of our revenues are earned by and paid to these VIEs. The equity interests in each of Gamease and Guanyou Gamespace are owned 60% by Tao Wang, our Chief Executive Officer, and 40% by Dewen Chen, our President. Mr. Wang and Mr. Chen are both PRC citizens. The equity interests in Shenzhen 7Road are owned by our VIE Gamease. The equity interests in Shanghai ICE are owned by two Changyou employees, Runa Pi and Rong Qi, who are PRC citizens and each of whom holds 50%.

Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE hold the licenses and permits required to operate our business and are controlled by AmazGame, 7Road Technology, Gamespace and ICE Information, respectively, through a series of contractual arrangements. AmazGame, 7Road Technology, Gamespace and ICE Information undertake substantially all of our product development and technical support functions, which they provide to Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE pursuant to contractual arrangements.

In the opinion of Haiwen & Partners, our PRC counsel, subject to the uncertainties and risks disclosed elsewhere in this annual report under the heading "Risk Factors" the ownership structures of our PRC subsidiaries and VIEs comply with all existing laws, rules and regulations of the PRC and each of such companies has the full legal right, power and authority, and has been duly approved, to carry on and engage in the business described in its business license.



The following diagram illustrates our corporate structure as of the date of this annual report.



→ Shareholding

--- Contractual arrangements among our WFOEs AmazGame, 7Road Technology, Gamespace and ICE Information, our VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE and their respective shareholders, which provide us with effective control over our VIEs. See “Major Shareholders and Related Party Transactions—Related Party Transactions—Contractual Arrangements with our VIEs and their Shareholders” in Item 7 of this annual report.

**ITEM 4A. UNRESOLVED STAFF COMMENTS**

Not applicable.

**ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS****MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*You should read the following discussion and analysis of our financial condition and results of operations in conjunction with the section entitled "Selected Consolidated Financial Data" and our consolidated financial statements and the related notes included elsewhere in this annual report. The discussion in this section contains forward-looking statements that involve risks and uncertainties. As a result of various factors, including those set forth under "Item 3. Key Information—Risk Factors" and elsewhere in this annual report on Form 20-F, our actual future results may be materially different from what we expect.*

**Overview**

We are a leading online game developer and operator in China as measured by the popularity of our MMOG TLBB and our Web games Wartune and DDTank, which we developed in-house. We engage in the development, operation and licensing of online games for PCs and mobile devices. This includes MMOGs, which are interactive online games that may be played simultaneously by hundreds of thousands of game players, Web games, which are played over the Internet using a Web browser, and mobile games, which are played on mobile devices and require an Internet connection. We also own and operate a number of Web properties and software applications for PCs and mobile devices (collectively referred to as "platform channels") related to games, including the 17173.com Website, one of the leading information portals for game players in China, the 37wanwan.com Website, a games portal that provides a collection of Web games to game players, and Raidcall, free social communication software that is used by professional and casual gamers. For the three months ended December 31, 2013, the games that we operate had approximately 25 million total average monthly active accounts, and our platform channels had approximately 149 million total average monthly active accounts.

TLBB is a popular martial arts MMORPG in China that is adapted from the popular Chinese martial arts novel "*Tian Long Ba Bu*," which means "*Novel of Eight Demigods*," written by the famous writer Louis Cha. Since TLBB's launch in May 2007, we have regularly developed new content and released game updates in the form of expansion packs for the game. TLBB has won various awards in China, including 2008 "Best Self-Developed Online Games (First Place)" and 2008 and 2009 "Most Liked Online Games by Game Players (First Place)" awards at the China Digital Entertainment Expo and Conference, or ChinaJoy. Its expansion packs, TLBB2, TLBB3 and New TLBB, won the 2010 "Most Liked Online Games by Game Players" award, the 2011 "Best Self-Developed Online Games" award, and the 2013 "Most Liked Online Games by Game Players" award, respectively, at ChinaJoy. TLBB was chosen as one of the 2012 "Most Liked Online Games by Game Players" at ChinaJoy. TLBB is currently licensed to third-party operators in Vietnam, Taiwan, Hong Kong, Malaysia and Thailand. We also operate a modified version of TLBB in the U.S.

DDTank is a popular 2D multi-player, combat and role-playing Web game in China. Game players control avatars to compete with other game players. Avatars can earn or buy various weapons, potions, magic rings, rockets and other items to increase competitiveness and enhance the game experience. Since DDTank's launch in March 2009, we have regularly released updates and more significant enhancements for the game. DDTank has won numerous game awards, including the "Baidu Outstanding Web Game" award in 2010 and 2012 and "One of the Top Ten Favorite Web Games" by the SAPPRFT in 2010 and 2011. DDTank was also the most searched-for casual Web game on Baidu.com for the 12 months ended each of June 30, 2012 and June 30, 2013, according to Baidu. We also jointly operate DDTank with third-party operators overseas. DDTank has been launched in 15 different language versions.

Wartune is a popular 2.5D role-playing and quasi real-time strategy Web game launched in December 2011 in China. Wartune is set in a mythical western universe where players build their own kingdoms in a virtual world where they must fight against a demonic race by developing their own villages and armies. Wartune won the "Baidu Outstanding Web Game" award in 2012 and the "Most Liked Web Games by Game Players" award at ChinaJoy in 2013. We also jointly operate Wartune with third-party operators overseas. Wartune has been launched in 15 different language versions.

We have several MMOGs, Web games and mobile games in our pipeline with different graphic styles, themes and features to appeal to different segments of the online game player community. Games in our pipeline, include, among others, a self-developed MMOG, YZZX; three licensed MMOGs, Echo of Soul, Asta, and Fantasy Frontier Online; two self-developed Web games, JY and SZHG; and several jointly-developed mobile games adapted from literary or other copyrighted works that we directly own or have acquired the exclusive rights to use from third-parties.

We also own and operate the 17173.com Website, a leading game information portal in China that provides news, electronic forums and other information services on online games to game players. The 17173.com Website was launched in 2000 as the first



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online game information portal in China, and is a leading online destination for game players seeking information on games and feedback from other players on the site's message boards. With over 750 game zones and tens of millions of monthly unique visitors supported by alliances with many thousands of Internet cafes, the 17173.com Website is one of the largest game information and community Websites in China and is widely recognized as a market leader among game Websites in China, with strong expertise in running the Website, building a game community and developing relationships with advertisers in the online game industry. As a result, the 17173.com Website is the marketing platform of choice for many online games, including our own. In addition, experienced game editors of the Website review and critique our games prior to launch, and we use the feedback received to improve the game quality of our games. We generate online advertising revenues from providing advertising services to third-party advertisers on the 17173.com Website. The 17173.com Website has won "Best Game Media" award for ten consecutive years from 2004 to 2013 at the Annual Game Industry Awards Gala.

We also own and operate in China and overseas other game-related platform channels, including the 17173.com Website; the 37wanwan.com Website, a games portal that provides a collection of Web games to game players; Raidcall, which is free social communication software that is used by professional and casual gamers; and other software applications that serve as access points to the 17173.com Website. The platform channels, as a whole, serve various needs of our game players and help us reach more game-player communities and conduct cross-promotions of our games and services, which in turn improve user loyalty.

Sohu.com Inc., our controlling shareholder, has operated a leading Chinese Internet portal, www.Sohu.com, since 1998. We have benefited from Sohu's strong brand recognition in China and large user base. Sohu's trusted brand name in China provides us with a broad marketing reach. By marketing across Sohu's Web domains and taking advantage of the Sohu Group's single-user ID system that provides easy access to our games, we believe we have been able to tap into Sohu's large user base to drive new users to our games. We intend to continue to leverage our relationships with Sohu in the development, marketing and operation of our games.





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We operate our current games under the item-based revenue model, meaning game players can play our games for free, but may choose to buy prepaid game cards that are used to pay for virtual items, which are non-physical items that game players can purchase and use within a game, such as gems, pets, fashion items, magic medicine, riding animals, hierograms, skill books and fireworks, to enhance the game-playing experience. For games that we operate, we mainly directly sell prepaid game cards to regional distributors and our game players in China through our online sales platform. Regional distributors sub-distribute prepaid game cards purchased from us to numerous retail outlets, including Internet cafés and various Websites, newsstands, software stores, book stores and retail stores. For games that we license to third-party operators, the licensee operators pay us an upfront license fee and we have revenue sharing rights over the duration of the license.

We continually collect feedback from our game players through multiple channels. Our product development team and our game operations team work closely together, allowing us to translate game player feedback into game updates and expansion packs in a timely manner. We typically release expansion packs, which are software packages that contain significant upgrades and improvements to a game based on the existing game's framework, every few months or as regularly as necessary based on game players' feedback, market demand and other factors. These upgrades may include new game content such as storylines, characters, tasks, maps and virtual items. We also update our games on a weekly basis with interim enhancements. We believe that such expansion packs and regular updates improve the game-playing experience and help to maintain the interest level of our game players, thereby helping us to extend the lifespan of our games.

Our revenues grew from \$484.6 million for the year ended December 31, 2011 to \$623.4 million for the year ended December 31, 2012, and to \$737.9 million for the year ended December 31, 2013, and our net income attributable to Changyou.com Limited grew from \$245.5 million for the year ended December 31, 2011 to \$282.4 million for the year ended December 31, 2012, and to \$268.6 million for the year ended December 31, 2013.

### ***Factors Affecting Our Results of Operations***

Our results of operations are affected by several key factors, including the following:

#### *General economic conditions affecting the online game, online advertising and cinema advertising industries in China*

We have benefited from general conditions typically affecting the online game, online advertising and cinema advertising industries in China, including the overall economic growth, which has resulted in increases in disposable income and discretionary consumer spending and increases in advertising spending; the increasing use of the Internet with the growth of personal computers and broadband penetration; the growing popularity of online games in comparison with other forms of entertainment; and favorable demographic trends, particularly the growth of the teenage and young adult population, who are typically more inclined to play online games. We cannot assure you that the Chinese economy will continue to grow, or that if there is growth, such growth will be steady and uniform and that any such growth will lead to growth in our online game business, our online advertising, or our cinema advertising business or that if there is a slowdown, such slowdown will not have a negative effect on those businesses. For example, a slowdown in China's economic growth that occurred between the first quarter of 2010 and the third quarter of 2012, caused in part by measures adopted by the Chinese government intended to slow such growth and to temper real estate prices and inflation, the significant instability recently experienced in the worldwide economy, with growth in the United States slowing, and the European Community facing disruptions as a result of crises in the economies of Greece and Spain, among other countries, and other such factors may lead in the future to decreases in the level of disposable income of our game players and negatively affect their spending on playing online games, as well as decreases in the advertising spending of our advertisers, who are typically other leading online game companies in China.

#### *Our ability to develop and maintain popular online games and convert our game player base into paying customers*

The popularity of our games drives the growth of our game player base, which is the key component driving the sales and consumption of our virtual items and thus our revenues. To maintain and grow the popularity of our games, we must diligently maintain the quality of the games and continually enhance the games to meet game player preferences and to incentivize game players to purchase virtual items. We solicit feedback from our game players and have a dedicated product development team that helps us to identify market trends and user preferences. For TLBB, we typically provide weekly updates and more substantial enhancements in the form of expansion packs every few months. We launch new virtual items to maintain game players' interest. We plan the timing of our new virtual item launches to avoid over-monetizing our existing game player base. We generally only launch virtual items after we have gained a certain number of new game players. If we fail to manage the growth of our game player base and manage our sales and marketing strategies for new virtual items, our game player base may not grow and we may not be successful in selling new virtual items, which would have an adverse effect on our revenues.



*The popularity and timing of the launch of new games*

We have in our pipeline several MMOGs, Web games and mobile games with different graphic styles, themes and features to appeal to different segments of the online game player community. Games in our pipeline, include, among others, a self-developed MMOG, YZZX; three licensed MMOGs, Echo of Soul, Asta, and Fantasy Frontier Online; two self-developed Web games, JY and SZHG; and several jointly-developed mobile games adapted from literary or other copyrighted works that we directly own or have acquired the exclusive rights to from third-parties.

*Product development and sales and marketing expenses*

Developing and marketing a new online game and maintaining its popularity in the market requires a commitment of significant resources, including product development and sales and marketing expenses. We typically incur such expenses several quarters before such games generate any revenues. If such games are not popular and do not generate substantial revenues, we may not be able to recover our product development and marketing expenses. In addition, because our product development strategy is to focus on a limited number of high-quality games, the failure of a small number of these games could adversely impact our growth rate.

We are currently making significant expenditures for the development of games and platforms for mobile devices such as phones and tablets. As a result, we expect to incur a net loss in the first quarter of 2014, and we may incur additional net losses in the future. If our mobile strategy is not successful, we may be unable to recoup those expenditures, and we may be unable to maintain or grow our revenues, or return to or sustain our historical levels of net income.

*The cost of attracting and retaining game development personnel*

Competition in the online game industry in China is intense, making it increasingly costly to retain and motivate existing talent and to attract new talent necessary for the growth of our business. Many of our competitors have been aggressively hiring game development personnel. If we are unable to retain our current talent and to attract new talent, we may have difficulty developing new games or enhancements for our existing games or meeting our development schedule, which could have an adverse impact on our business, financial condition and results of operations. See “Risk Factors—Risks Related to Our Business and Our Industry—Our business may not succeed in a highly competitive market” in Item 3.

*Any restrictions imposed by PRC law on payments from VIEs to our subsidiaries pursuant to contractual arrangements and any increase in the amount of PRC taxes applicable to such payments may adversely affect our business.*

We conduct a substantial portion of our operations through our VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, which generate substantially all of our revenues. As our VIEs are not owned by our subsidiaries, they are not able to make dividend payments to our subsidiaries. Instead, AmazGame, 7Road Technology, Gamespace and ICE Information, our subsidiaries in China, entered into a number of contracts with their corresponding VIEs, pursuant to which the VIEs pay the PRC subsidiaries for certain services that the PRC subsidiaries provide to their corresponding VIEs. However, depending on the nature of services provided, certain of these payments are subject to PRC taxes at different rates, including business taxes and VAT, which effectively reduce the amount that we receive from the VIEs. We cannot assure you that the PRC government will not impose restrictions on such payments or change the tax rates applicable to such payments. Any such restrictions on such payments or increases in the applicable tax rates may adversely affect our ability to receive payments from the VIEs or the amount of such payments.

*Government regulation imposed on online game industry*

The Chinese government is formulating new regulations to further strengthen supervision of the online game industry. These regulations may increase our compliance costs, delay the release of our new games and new expansion packs for existing games, and restrict the access of certain groups of players, such as minors, to our games, which in turn may significantly affect our operating results. See “Risk Factors—Risks Related to Our Business and Our Industry.”



### Our Revenues

The following table sets forth the revenues generated from our online games, online advertising and others revenues, in absolute amounts and as a percentage of total revenues for the periods indicated:

	For the Year Ended December 31,					
	2011		2012		2013	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	% of Total Revenues
(\$ in thousands except percentages)						
<b>Revenues:</b>						
Online game	435,512	89.9%	570,346	91.5%	669,168	90.7%
Online advertising	36,349	7.5%	42,525	6.8%	49,998	6.8%
IVAS	1,862	0.4%	4,307	0.7%	5,402	0.7%
Others	10,853	2.2%	6,251	1.0%	13,307	1.8%
Total revenues	484,576	100.0%	623,429	100.0%	737,875	100.0%

The following table sets forth certain operating data for our business in China for the periods indicated:

	For the Three Months Ended				
	December 31, 2012	March 31, 2013	June 30, 2013	September 30, 2013	December 31, 2013
Average Monthly Active Accounts of our Games (in millions)(1)	38	37	36	31	25
Average Monthly Active Accounts of our Platform Channels (in millions)(2)	77	85	85	99	149

- (1) Calculated as the simple average of the sum of monthly active accounts of all of our MMOGs, Web games and mobile games operated by us during the specified quarter. Monthly active accounts for our games are defined as game accounts that were logged in at least once during the month.
- (2) Calculated as the simple average of the sum of the monthly unique visitors to our Web game operation platform, the 17173 Website and 17173's non-game products, plus the monthly logged-in accounts of non-game applications during the quarter.

Our calculation of average monthly active accounts of our games and average monthly active accounts of our platform channels may not be comparable to similarly-named measures presented by other online game companies.

Total average monthly active accounts of the Company's games in the fourth quarter of 2013 were 25 million, a decrease of 34% year-over-year. The decrease was mainly driven by a decline in active accounts of TLBB after the Company closed down certain game accounts during the year so as to further enhance the balance of the in-game economic system, a decline in active accounts of DDTank as the game has entered into a relatively mature phase, and a decline in active accounts of Wartune in China.

Total average monthly active accounts of the Company's platform channels in the fourth quarter of 2013 were 149 million, an increase of 94% year-over-year. The increase was mainly due to the promotion, acquisition and launch of multiple software applications for PCs and mobile devices in 2013.

### Online Game Revenues

Online game revenues include revenues from MMOG operations, Web games and overseas licensing.

We disclosed in our previous annual reports the following operational metrics for our games: aggregate registered accounts, aggregate peak concurrent users, aggregate active paying accounts and aggregate revenue per active paying account, or ARPU. However, given the diversified business we currently operate, those previous operational metrics are no longer the most relevant metrics for measuring the existing positioning and future growth of our business. In order to provide you with a better foundation for understanding our performance as a whole across all the different products and services that we offer, starting with 2013, we discontinued disclosure of those previous operational metrics and introduced two new operational metrics: total average monthly active accounts of our games and total average monthly active accounts of our platform channels.



### *MMOG operations*

All of our MMOGs currently in operation in China are free to play games that generate revenues using the item-based revenue model through the sale of virtual items that enhance the game-playing experience. Game players can purchase virtual items, such as gems, pets, fashion items, magic medicine, riding animals, hierograms, materials, skill books and fireworks by purchasing prepaid game cards or game points.

### *Web games*

We began generating Web game revenue after our acquisition of a controlling interest in 7Road in May 2011. 7Road is the developer and creator of Wartune and DDTank, two of China's most popular Web games. The game is free to play and generates revenues using the item-based revenue model through the sale of virtual items that enhance the game-playing experience. 7Road jointly operate these games with third-party operators who offer the games to users in China and other countries and administrative regions on their Websites or platforms. 7Road also directly operates Wartune and DDTank on its own Websites for the games.

### *Overseas licensing*

To leverage the success of our popular in-house developed games, we license our MMOGs to third-party operators in overseas countries or administrative regions. These licensing agreements provide two revenue streams, consisting of an initial license fee and a monthly revenue-based royalty fee based on monthly revenue and sales from ancillary products of the games.

### Online Advertising Revenues

Online advertising revenues are generated from the 17173 Business, which provides online advertising services on our 17173.com Website. A contract is signed to establish a fixed price and the advertising services to be provided. Based on the contracts, the 17173 Business provides advertisement placements on its Websites and/or in different formats, including, among other things, banners, links, logos, buttons, rich media and content integration.

### IVAS Revenues

We offer Web games developed by third-party developers and generate revenues from the provision of IVAS, including promotion, access maintenance and payment services, to third-party developers. Under revenue-sharing agreements that we sign with third-party developers, we collect payments from the end users, keep a pre-agreed percentage of the proceeds and remit the balance to the third-party developers. Revenues from IVAS are recognized when our obligations under the agreements and all other revenue recognition criteria have been met. Revenues from IVAS are recognized under the gross method, as we are the principal obligor for provision of the services.

### Others Revenues

Others revenues consist of cinema advertising revenues, which we began generating after we acquired the remaining 50% of the equity interests in each of Shanghai Jingmao and Shanghai Hejin and became the sole shareholder of these two companies in January 2011. We provide clients advertising placements on slots that are shown in theatres before the screening of movies. The rights to place advertisements in such advertising slots are granted under contracts with different theatres and film production companies.

## ***Revenue Collection***

### Online Game Revenues

#### *MMOG operations*

We sell virtual and physical prepaid game cards to regional distributors, who in turn sub-distribute to retail outlets, including Internet cafés, various Websites, newsstands, software stores, bookstores and retail stores. We typically collect payment from our distributors upon delivery of our prepaid game cards, but only recognize revenues as the virtual items are consumed. We generally offer a sales discount to our prepaid game card distributors based on the popularity of our games. In 2008, we offered an initial sales discount at a rate of 15.0%, which decreased to a rate of 11.0%, effective as of January 2009, a rate of 10.0%, effective as of January 2011, a rate of 9.0%, effective as of January 2012 and to the current rate of 2%, effective October 1, 2013. In addition, we previously offered a discount of 5.0% to our game players who directly purchased virtual prepaid game cards and game points from our online sales system, but we discontinued the discount effective September 23, 2013. The discount represented the difference between the price at which we sold prepaid game cards to distributors or game players, as the case may be, and the face value of the prepaid game cards or the equivalent of game points.



We also offer rebates in the form of credits on future purchases of prepaid game cards to distributors of our prepaid game cards. Distributors of prepaid game cards receive a credit on future purchases of our prepaid game cards, provided that the distributors meet certain preset sales conditions. Prior to October 1, 2013, we offered a credit rate equal to 1% to 3% of the discounted value of our prepaid game cards. In October, 2013, we decreased the maximum rate from 3% to 2%. Historically, most of our distributors have met the conditions required to receive these credits. Credits are in the form of free prepaid game cards. We incur transaction costs of 0.1% to 0.5% of the face value of the virtual prepaid game cards or the equivalent of game points by using third-party payment platforms.

Before October 2013, the total discount and rebate rate we typically offered to all of our prepaid game card distributors was approximately 10.0% to 12.0% of the face value of our prepaid game cards. Effective in October 2013 the total discount and rebate rate is approximately 4%. Prior to September 2013, the total discount and transaction costs associated with game players' use of third-party payment platforms was 5.1% to 5.5% of the face value of the virtual prepaid game cards or the equivalent of game points purchased. In September 2013, we lowered the rate to 0.1% to 0.5%.

#### *Web games*

We generate revenues from our Web games, such as Wartune and DDTank, primarily from joint operation of the games with third-party joint operators through their Websites and platforms in China and overseas. All of the third-party joint operators of our Web games make payments to us based on a percentage of the revenues they generate from the games. Beginning in May 2012, we also generated revenues from direct operation of Wartune and DDTank through our own Websites for the games. Certain of our joint operators pay us license fees for the exclusive right to operate our games in specified geographic areas, upon achievement of certain revenue milestones from their operation of our games. Certain of the joint operators also pay us license fees for the right to be among a selected few who will have the initial right ahead of other operators to jointly operate our games in China during a specified period after their launch.

#### *Overseas licensing*

Our overseas licensing revenues consist of an initial license fee and ongoing revenue-based royalties. The initial license fee includes a fixed amount payable upon signing the license agreement and additional license fees payable upon achieving certain sales targets. The ongoing revenue-based royalties are generally determined based on the amount charged to game players' accounts and sales of ancillary products of the game. We typically receive ongoing revenue-based royalties on a monthly basis.

#### Online Advertising Revenues

Online advertising revenues are generated from our operation of the 17173 Business, which provides online advertising services on our 17173.com Website. We sell advertising placements either through advertising agencies or directly to customers. We typically require customers to pay 6.4% to 10.0% of the contract amounts, upon entering into the contracts, as deposits to secure their obligations to us under the contracts. Such deposits reduce the receivables under the contracts, and are repayable on demand when a customer terminates its relationship with the 17173 Business.

#### IVAS Revenues

We offer Web games developed by third-party developers and generate revenues from the provision of IVAS, including promotion, access maintenance and payment services, to third-party developers. Under revenue-sharing agreements that we sign with third-party developers, we collect payments from the end users, keep a pre-agreed percentage of the proceeds and remit the balance to the third-party developers.

#### Others Revenues

Others revenues consist of cinema advertising revenues. We sell cinema advertising slots primarily through advertising agencies. We charge most advertisers on a per-advertising slot basis or on a pre-determined period basis with fixed fees. Our standard prices for advertising slots vary depending on the location of the cinemas. Discounts from standard rates are typically provided for longer-term advertising contracts, and may be provided for promotional purposes.





## ***Revenue Recognition***

### **Online Game Revenues**

Online game revenues include our MMOG operations, Web game and overseas licensing revenues.

#### ***MMOG operations***

We earn revenues through providing MMOGs to players pursuant to the item-based revenue model. Under the item-based model, the basic game play functions are free of charge and players are charged for purchases of in-game virtual items.

MMOG operations revenues are collected by our VIEs through the sale of our prepaid cards, which it sells in both virtual and physical forms to third-party distributors and players. Proceeds received from sales of prepaid cards are initially recorded as receipts in advance from customers and, upon activation or charge of the prepaid cards, are transferred from receipts in advance from customers to deferred revenues. As we do not have control of, and generally do not know, the ultimate selling price of the prepaid cards sold by distributors, net proceeds from distributors form the basis of revenue recognition.

Under the item-based revenue model, revenue is recognized over the estimated lives of the virtual items purchased or when the virtual items are consumed. If different assumptions were used in deriving the estimated lives of the virtual items, the timing of our recording of revenues would be impacted.

Revenues are recorded net of business tax, discounts and rebates to distributors.

Prepaid cards will expire two years after the date of card production if they have never been activated. The proceeds from expired prepaid cards are recognized as revenue upon expiration of the cards.

Once the prepaid cards are activated and credited to a player's personal game account, they will not expire as long as the personal game account remains active. We are entitled to terminate a player's personal game account if it has been inactive for a period of 180 consecutive days. The unused balances in an inactive player's personal game account are recognized as revenues when the account is terminated.

For the years ended December 2013, 2012 and 2011, we recognized revenues in connection with expired un-activated prepaid cards and unused balances in inactive accounts of approximately \$951,000, \$627,000 and \$964,000, respectively.

#### ***Web Games***

We began generating Web game revenue after our acquisition of a controlling interest in 7Road in May 2011. Revenues from our Web games are derived mainly from revenue-sharing payments from third-party joint operators of our games and license fees from certain of these joint operators. We also derive revenues from direct operation of Wartune and DDTank on our own Websites for the games. Web games are operated primarily under the item-based revenue model, in which game players can access the games free of charge, but may purchase consumable virtual items, including those with a predetermined expiration time, or perpetual virtual items, such as certain costumes that stay bound to a game player throughout the life of the game. In certain of our joint operation arrangements, we provide our games and related services to a third-party joint operator at no upfront fee. In these arrangements, we are entitled to a single stream of revenue-sharing payments from the joint operator when game players convert the joint operator's virtual currency into our game coins or purchase its game coins directly through such operator's Website or game platform. Certain of the joint operators pay us license fees for the exclusive right to operate its games in specified geographic areas or upon achievement of certain performance milestones from the joint operators' operation of the games. Certain of the joint operators also pay us license fees for the right to be among a selected few who will have the initial right ahead of other operators to jointly operate our games in China during a specified period after their launch.

When our games are jointly operated through the Websites or platforms of third-party joint operators, the games may be hosted either on the third-party operators' servers or on servers that we own or lease from Internet data centers. In our arrangements with third-party joint operators, we view the third-party joint operators as our customers and do not view ourselves as the primary obligors, as we do not have the primary responsibility for fulfillment and acceptability of the game services. For direct operation of Wartune and DDTank through our Websites for the games, we are obligated to provide on-going services to the game players, and such obligation is not deemed to be inconsequential and perfunctory after game players purchase our game coins directly through our Websites for the games. Therefore, revenues from direct operation of Wartune and DDTank on our Websites for the games are first recorded by us as deferred revenues and subsequently recognized as revenue over the service period during which we are obligated to provide services to the game players to enable them to consume their virtual items.



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PRC tax authorities have determined that all of the game revenues from the joint operation of our Web games within China, which are generated through Shenzhen 7Road, are subject to 17% PRC VAT, and that Shenzhen 7Road, as a “software enterprise,” is entitled to a 14% VAT refund immediately upon the filing of its VAT returns, with the result that Shenzhen 7Road’s net effective PRC VAT rate is 3%. Shenzhen 7Road presents PRC VAT on a gross basis, by which VAT at the rate of 17% is included in revenues, and Shenzhen 7Road’s net effective PRC VAT rate of 3% is included in cost of revenues, because Shenzhen 7Road’s 17% VAT obligation and its entitlement to a 14% VAT refund are one integrated preferential VAT policy. The amounts of PRC VAT included in our revenues for the year ended December 31, 2013, December 31, 2012 and for the period between May 11, 2011, which was the date of our acquisition of a controlling interest in Shenzhen 7Road, and December 31, 2011, were \$9.3 million, \$8.8 million and \$1.9 million, respectively.

#### Overseas licensing

We enter into licensing arrangements with third-party operators to operate our MMOGs in other countries and regions. These licensing agreements provide two revenue streams, consisting of an initial license fee and a monthly revenue-based royalty fee based on monthly revenue and sales from ancillary products related to the games. The initial license fee is based on both a fixed amount and additional amounts receivable upon the game’s achieving certain sales targets. Since we are obligated to provide post-sales services, such as technical support and provision of updates and when-and-if-available upgrades to the licensees during the license period, the initial license fee from the licensing arrangement is recognized as revenue ratably over the license period. The fixed amount of the initial license fee is recognized ratably over the remaining license period from the launch of the game and the additional amount is recognized ratably over the remaining license period from the date such additional amount is certain. The monthly revenue-based royalty fee is recognized when relevant services are delivered, provided that collectability is reasonably assured.

#### Online Advertising Revenues

Online advertising revenues are generated from the 17173 Business. A contract is signed with the advertiser establishing a fixed price and the advertising services to be provided. Based on the contracts, the 17173 Business provides advertisement placements on its Websites and/or in different formats, including banners, links, logos, buttons, rich media and content integration.

To determine the method of recognition of online advertising revenue, prior to entering into contracts, management makes a credit assessment of the customer to assess the collectability of the contract. For those contracts for which the collectability is determined to be reasonably assured, revenue is recognized ratably over the period during which the advertising services are provided and when all revenue recognition criteria are met. For those contracts for which the collectability is determined not to be reasonably assured, revenue is recognized only when the cash is received and all other revenue recognition criteria are met.

Before 2011, the 17173 Business treated multiple deliverable elements of advertising contracts as a single unit of accounting for revenue recognition purposes. On January 1, 2011, in accordance with ASU No.2009 -13, the 17173 Business began to treat advertising contracts with multiple deliverable elements as separate units of accounting for revenue recognition purposes and to recognize revenue on a periodic basis during the contract periods when each deliverable service was provided. Since the contract price is for all the deliverables under an advertising contract, the 17173 Business allocates the contract price among all the deliverables at the inception of the arrangement on the basis of their relative selling prices according to the selling price hierarchy established by ASU No.2009 -13. The 17173 Business first uses vendor-specific objective evidence of selling price, if it exists. If vendor-specific objective evidence of selling price does not exist, the 17173 Business uses third-party evidence of selling price. If neither vendor-specific objective evidence of selling price nor third-party evidence of selling price exists, the 17173 Business uses management’s best estimate of the selling price for the deliverable.

A pilot program for transition from the imposition of PRC business tax, or Business Tax, to the imposition of VAT for revenues from certain industries, or the Pilot Program, was launched in Shanghai on January 1, 2012. Starting from September 1, 2012, the Pilot Program was expanded from Shanghai to eight other cities and provinces in China, including Beijing. Our online advertising revenues became subject to the Pilot Program on September 1, 2012 and are now subject to VAT, instead of Business Tax, at a rate of 6%. Online advertising revenues are recognized after deducting agent rebates and net of VAT and related surcharges.



### IVAS Revenues

We offer Web games developed by third-party developers and generate revenues from the provision of IVAS, including promotion, access maintenance and payment services, to third-party developers. Under revenue-sharing agreements that we sign with third-party developers, we collect payments from the end users, keep a pre-agreed percentage of the proceeds and remit the balance to the third-party developers. Revenues from IVAS are recognized when our obligations under the agreements and all other revenue recognition criteria have been met. Revenues from IVAS are recognized under the gross method, as we are the principal obligor with respect to provision of the services

### Others Revenues

Others revenues are composed of cinema advertising revenues.

For cinema advertising revenues, a contract is signed with the advertiser to establish a fixed price and specify advertising services to be provided. Based on the contracts, we provide advertisement placements in advertising slots to be shown in theatres before the screening of movies. Revenue from cinema advertising is recognized when all the recognition criteria are met. Depending on the terms of a customer contract, fees for services performed can be recognized according to two principal methods, which are the proportional performance method and the straight-line method. Under the proportional performance method, fees are generally recognized based on a percentage of the advertising slots actually delivered where the fee is earned on a per-advertising slot placement basis. Under the straight-line method, fees are recognized on a straight-line basis over the contract period when the fee is not paid based on the number of advertising slots actually delivered.

### *Cost of Revenues*

Cost of online game revenues consists primarily of salary and benefits, bandwidth leasing charges, depreciation expenses, revenue-based royalty payments to the game developers, business taxes and value-added taxes arising primarily from the revenues that AmazGame and Gamespace derive from their contractual arrangements with Gamease and Guanyou Gamespace, respectively, amortization of licensing fees, and other direct costs.

Cost of online advertising revenues mainly consists of salary and benefits, bandwidth leasing costs, and depreciation expenses.

Cost of others revenues mainly consists of payments to theatres and film production companies for pre-film screening advertising slots.

Total cost of revenues increased to \$126.4 million for the year ended December 31, 2013 compared to \$104.5 million and \$67.5 million, respectively, for the years ended December 31, 2012 and 2011. The increase in cost of revenues is primarily due to an increase in salary and benefits expenses, bandwidth leasing and communication costs, content and license fees, revenue-based royalty payments to game developers, and PRC business taxes and VAT paid by AmazGame, Gamespace and Shenzhen 7Road in line with the increase in revenues; We expect that the cost of revenues will increase in the future as we continue to expand our game portfolio.

### *Operating Expenses*

Our operating expenses consist of product development expenses, sales and marketing expenses, general and administrative expenses, and goodwill impairment and impairment of intangibles via acquisitions of businesses. Share-based compensation expenses are included in product development expenses, sales and marketing expenses, and general and administrative expenses. We expect that our operating expenses will increase in the future as we expand our research and development workforce to design and develop new MMOGs, Web games and mobile games, in addition to rolling out our plan to transform the 17173.com Website into a one-stop-shop platform for online game players in China. Further, we plan to carry out more marketing activities to promote our existing and new online game products, the 17173 Business and our platform channels.



The following table sets forth our product development expenses, sales and marketing expenses, general and administrative expenses, and goodwill impairment and impairment of intangibles via acquisitions of businesses, both in absolute amount and as a percentage of total revenues for the periods indicated:

	For the Year Ended December 31,					
	2011		2012		2013	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	% of Total Revenues
	(\$ in thousands, except percentages)					
Product development	52,238	10.8%	73,755	11.8%	119,909	16.3%
Sales and marketing	49,893	10.3%	60,639	9.7%	128,830	17.5%
General and administrative	29,684	6.1%	33,514	5.4%	57,191	7.8%
Goodwill impairment, impairment of intangibles via acquisitions of businesses	5,420	1.1%	2,906	0.5%	—	—
Total	137,235	28.3%	170,814	27.4%	305,930	41.6%

#### *Product Development Expenses*

Our product development expenses consist primarily of salary and benefits expenses, including share-based compensation expenses, of personnel engaged in the development of our game development platform and our games, and content and license expenses relating to our games. Product development expenses increased to \$119.9 million for the year ended December 31, 2013 compared to \$73.8 million and \$52.2 million, respectively, for the years ended December 31, 2012 and 2011. The increase in such expenses is primarily due to our increased research and development workforce and an increase in licensing fees incurred in 2013 for games that we licensed from third parties. Product development expenses constituted 16.3%, 11.8% and 10.8% of our total revenues for the years ended December 31, 2013, 2012 and 2011, respectively.

#### *Sales and Marketing Expenses*

Our sales and marketing expenses consist primarily of expenses for advertisement and promotion, and salary and benefits expenses, including share-based compensation expenses, of our sales and marketing personnel. Sales and marketing expenses increased to \$128.8 million for the year ended December 31, 2013 compared to \$60.6 million and \$49.9 million for the years ended December 31, 2012 and 2011. The increase was mainly because of higher advertising costs for the promotion of software applications for PCs and mobile devices as part of our initiative to develop our platform business, and higher advertising costs for the promotion of TLBB and new mobile games and an increase in salary and benefits expenses in 2013. Sales and marketing expenses constituted 17.5%, 9.7%, and 10.3% of our total revenues for the years ended December 31, 2013, 2012 and 2011, respectively.

#### *General and Administrative Expenses*

Our general and administrative expenses consist primarily of salary and benefits expenses, including share-based compensation expenses, for management, finance and administrative personnel, and professional service fees, such as audit fees and fees for tax consultation. General and administrative expenses increased to \$57.2 million for the year ended December 31, 2013 compared to \$33.5 million and \$29.7 million for the years ended December 31, 2012 and 2011. This increase was primarily due to (i) an increase in headcount and related salary and benefits expenses in 2013; (ii) an increase in professional fees in 2013. General and administrative expenses constituted 7.8%, 5.4% and 6.1% of our total revenues for the years ended December 31, 2013, 2012 and 2011, respectively.

#### *Goodwill impairment and impairment of intangibles via acquisitions of businesses*

We did not incur any impairment loss for the year ended December 31, 2013, compared to an impairment loss of \$2.9 million for the year ended December 31, 2012, which primarily comprised impairment of intangibles via acquisitions of businesses, and an impairment loss of \$5.4 million for the year ended December 31, 2011, which primarily comprised impairment of goodwill of \$5.2 million arising from our acquisition of the cinema advertising business, and impairment of an acquired tradename of \$0.2 million.



## *Share-based Compensation Expenses*

### Changyou share-based awards

Share-based compensation expenses for periods prior to the completion of our initial public offering included in our financial statements include an allocation to us of such expenses related to Sohu's senior management who provide services for both Sohu and Changyou. Following completion of our initial public offering, Sohu's management did not continue to provide these services and therefore our financial statements do not include such allocations for periods after the completion of the offering.

In March 2005, Sohu formed an indirect subsidiary to carry out game development, and granted to Tao Wang, who at the time was an employee of Sohu, a contingent right to receive a payment equal to 25% of the value of the subsidiary upon the occurrence of certain events. Sohu later agreed with Mr. Wang that his contingent right in the subsidiary would be modified to provide Mr. Wang an equity interest in us in lieu of the contingent right.

In January 2008, we communicated to and agreed with Mr. Wang that the equity interest we granted to him would consist of 7,000,000 of our ordinary shares and 8,000,000 restricted shares. The terms of the restricted shares included, as a condition of vesting, the completion of an initial public offering by us on an internationally recognized stock exchange, and also were subject to a vesting schedule. In addition, the terms of the restricted shares provided that Mr. Wang would not be entitled to participate in any distributions by us on his ordinary shares and restricted shares until the completion of our initial public offering. In April 2008, we modified the vesting conditions of the restricted shares to provide for vesting over a four-year period, subject to acceleration under certain circumstances, commencing on February 1, 2008, with no condition that an initial public offering be completed. There was no change, however, to the limitation on Mr. Wang's right to participate in distributions declared by us prior to the completion of our initial public offering.

On December 31, 2008, we reserved 20,000,000 of our ordinary shares to be used as incentive compensation for our executive officers and key employees from time to time under our 2008 Share Incentive Plan.

On January 15, 2009, 7,000,000 Class B ordinary shares and 8,000,000 Class B restricted shares were issued to Mr. Wang out of Sohu's equity interest. The difference between the fair values, or the Incremental Fair Value, of the 7,000,000 Class B ordinary shares and 8,000,000 Class B restricted shares granted to Mr. Wang and Mr. Wang's contingent right in the Sohu subsidiary is accounted for by us as share-based compensation. Because the terms of the issuance of the ordinary shares and restricted shares had been approved by us and were communicated to and agreed with Mr. Wang as of January 2, 2008, that date was deemed as the grant date under U.S. GAAP and, accordingly, the Incremental Fair Value was determined as of that date. The portion of the Incremental Fair Value related to the 7,000,000 Class B ordinary shares, equal to \$1.8 million, was recognized as share-based compensation expenses included in product development expenses for the three months ended March 31, 2008. As a result of the modification of the vesting terms of the 8,000,000 Class B restricted shares on April 21, 2008, the portion of the Incremental Fair Value related to those shares, equal to \$7.0 million, was determined as of that date and is accounted for by us as share-based compensation over the vesting period starting from the date of the modification, following the accelerated basis of attribution. Share-based compensation expense relating to the 8,000,000 Class B restricted shares, which was \$nil for the year ended December 31, 2013, \$41,000 for the year ended December 31, 2012 and \$0.5 million for the year ended December 31, 2011, was included as share-based compensation expenses included in product development expenses. The Incremental Fair Values were determined using the discounted cash flow method.

In April 2008, our Board of Directors approved and we communicated to our executive officers other than the CEO and to certain employees, various grants of restricted shares and restricted share units. Pursuant to these approvals, on January 15, 2009, we issued to our executive officers other than the CEO an aggregate of 1,800,000 Class B restricted shares and we issued to certain of our key employees an aggregate of 940,000 restricted share units (setttable in Class B ordinary shares). On March 13, 2009, we exchanged the 1,800,000 Class B restricted shares held by executive officers other than the CEO for Class B restricted share units which have the same vesting and other terms as applied to the Class B restricted shares. The vesting of the restricted share units was contingent upon the completion of an initial public offering by us on an internationally recognized stock exchange, and is otherwise subject to vesting over a four-year period, subject to acceleration under certain circumstances, commencing February 1, 2008. As of December 31, 2013, of these 2,740,000 restricted share units granted 2,665,000 restricted share units were vested and settled and 75,000 restricted share units had been forfeited. The grant date fair value of the awards is recognized in our consolidated statements of operations starting from the date when the vesting conditions became probable, which occurred upon the completion of our initial public offering. The fair values of these awards, which total \$5.4 million, were determined using the discounted cash flow method. Share-based compensation expense relating to these 2,740,000 restricted share units, which was \$nil, \$31,000 and \$0.4 million, respectively, for the years ended December 31, 2013, 2012 and 2011, following the accelerated basis of attribution, were included in operating expenses.





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On February 17, 2009, we granted an aggregate of 456,000 Class A restricted share units (setttable upon vesting in Class A ordinary shares) to certain of our employees. The fair value of these restricted share units, which is \$3.6 million, was determined using our initial public offering price. The vesting of the restricted share units is contingent upon the completion of an initial public offering by us on an internationally recognized stock exchange, and such restricted shares are otherwise subject to vesting over a four-year period, subject to acceleration under certain circumstances, commencing on February 17, 2009. Share-based compensation expense relating to these restricted share units, which was negative \$0.3 million, \$0.3 million and \$0.6 million, under an estimated forfeiture rate of 10%, for the years ended December 31, 2013, 2012 and 2011, was included in operating expenses. The negative \$0.3 million for the year ended December 31, 2013 represented our true-up of the share-based compensation expense for restricted share units forfeited in 2013. As of December 31, 2013, 88,128 Class A restricted share units of such 456,000 Class A restricted share units had been forfeited.

On April 21, 2009, we granted an aggregate of 1,200,000 Class A restricted share units (setttable upon vesting in Class A ordinary shares) to executive officers other than our CEO. The fair value of these restricted share units, which is \$14.9 million, was determined using the grant-day market price as a key factor. These restricted shares are subject to vesting over a four-year period commencing on April 21, 2009. Share-based compensation expense relating to these restricted share units, which was \$0.3 million, \$1.3 million and \$2.7 million, respectively, for the years ended December 31, 2013, 2012 and 2011, was included in operating expenses, following the accelerated basis of attribution.

As of December 31, 2013, we had granted an aggregate of 367,552 Class A restricted share units (setttable upon vesting in Class A ordinary shares) to certain of our employees. The fair value of these restricted share units, in an aggregate amount of \$5.2 million, was determined using the grant-day market price as a key factor. These restricted shares are subject to vesting over a four-year period commencing on the grant date. Share-based compensation expense relating to these restricted share units for the years ended December 31, 2013, 2012 and 2011 of \$1.1 million, \$1.5 million, and \$0.8 million, respectively, based on an estimated forfeiture rate of 10%, was included in operating expenses following the accelerated basis of attribution. As of December 31, 2013, 24,150 Class A restricted share units of such 367,552 Class A restricted share units that had been granted had been forfeited.

For the year ended December 31, 2010 and 2011, we granted 40,000 and 20,000, respectively, Class A restricted share units (setttable upon vesting in Class A ordinary shares) to certain employees of the 17173 Business, which was then owned and operated by Sohu, for their involvement in the provision of certain online game links and advertising services to us on Sohu's Websites. These Class A restricted share units are subject to vesting over a four-year period commencing on the grant date. Since we completed the acquisition from Sohu of certain assets associated with the 17173 Business in December, 2011, we have accounted for the Class A restricted share units granted to employees of the 17173 Business as share awards granted to our employees. Share-based compensation expense relating to these restricted share units for the years ended December 31, 2013, 2012 and 2011 in the amount of \$0.1 million, \$0.3 million and \$0.5 million, respectively, was included in operating expenses following the accelerated basis of attribution. As of December 31, 2013, 13,000 previously granted Class A restricted share units had been forfeited.

Share-based compensation expenses recorded for the year ended December 31, 2013 were \$1.3 million compared to \$3.7 million and \$6.1 million for the year ended December 31, 2012 and 2011, and include share-based compensation paid by us to our executive officers and other employees, allocated share-based compensation paid by Sohu to Sohu's senior management who provided services to both Sohu and the 17173 Business prior to our acquisition of the 17173 Business, and share-based compensation related to options and restricted share units granted by Sohu to our employees. These share-based compensation expenses have been allocated to (i) cost of revenues, (ii) sales and marketing expenses, (iii) general and administrative expenses and (iv) product development expenses, depending on the responsibilities of the relevant employees.

As of December 31, 2013, there was no unrecognized share-based compensation cost related to the 8,000,000 unvested Class B restricted shares granted to our CEO in January 2009; no unrecognized share-based compensation cost related to the 1,800,000 unvested Class B restricted share units granted to our executive officers other than our CEO in April 2008 (whose Class B restricted shares were exchanged for Class B restricted share units (setttable in Class B ordinary shares) on March 13, 2009); no unrecognized share-based compensation cost related to the 940,000 unvested Class B restricted share units granted to certain of our key employees in April 2008; no unrecognized share-based compensation cost related to the 456,000 unvested Class A restricted share units granted to certain of our employees in February 2009; no unrecognized share-based compensation cost related to the 1,200,000 unvested Class A restricted share units granted to executive officers other than our CEO in April 2009; \$1.2 million of unrecognized share-based compensation cost related to the 367,552 unvested Class A restricted share units granted to certain employees in 2010, 2011, 2012 and 2013, net of estimated forfeitures; and \$0.1 million of unrecognized share-based compensation cost related to the 60,000 unvested Class A restricted share units granted to employees of the 17173 Business in 2010 and 2011.



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7Road share-based awards

On July 10, 2012, 7Road adopted a 2012 Share Incentive Plan (the “7Road 2012 Share Incentive Plan”), which initially provided for the issuance to selected directors, officers, employees, consultants and advisors of 7Road of up to 5,100,000 ordinary shares of 7Road (amounting to 5.1% of the then outstanding 7Road shares on a fully-diluted basis). On November 2, 2012, 7Road’s Board of Directors and its shareholders approved an increase from 5,100,000 to 15,100,000 ordinary shares (amounting to 13.7% of the then outstanding 7Road shares on a fully-diluted basis) under the 7Road 2012 Share Incentive Plan.

On May 1, 2013, Changyou entered into an agreement to acquire all of the outstanding ordinary shares of 7Road held by the non-controlling shareholders, representing 28.074% of the outstanding share capital of 7Road. The acquisition closed on June 5, 2013.

On June 28, 2013, 7Road’s Board of Directors approved the cancellation of the 7Road 2012 Share Incentive Plan. 7Road concurrently offered to a total of 42 7Road employees holding an aggregate of 2,223,750 restricted share units which had been granted under the 7Road 2012 Share Incentive Plan the right to exchange their restricted share units for, at each employee’s election, in each case subject to the employee’s continued employment by 7Road, either (i) the right to a cash payment of up to an aggregate of \$2.90 per restricted share unit exchanged, vesting and payable at the rate of 40%, 30% and 30%, respectively, on the first, second and third anniversaries of July 18, 2012, which is the date when the surrendered restricted share units were granted under the 7Road 2012 Share Incentive Plan, or (ii) the right to receive an annual cash bonus, over a seven-year period commencing July 1, 2013, based on adjusted annual cumulative net income of 7Road. All restricted share units held by these 42 holders under the 7Road 2012 Share Incentive Plan as of June 28, 2013 were included in this exchange program.

As the original awards of restricted share units made under the 7Road 2012 Share Incentive Plan included as a vesting condition the completion of an initial public offering, which is not considered probable under it occurs, no share-based compensation expense was recognized for the fair value of the original awards. As of the date of the modification resulting from the exchange program, incremental compensation expense, which is not classified as share-based compensation expense, will be the fair values of the two new compensation schemes included in the exchange program.

For Scheme I, the modification resulted in total incremental compensation expense of \$5.7 million, which will be recognized in the consolidated statements of comprehensive income ratably over the remaining vesting period of the awards for each tranche. For fiscal year 2013, compensation expense of \$3.3 million was recognized in the consolidated statements of comprehensive income. In 2013, 7Road paid \$1.6 million in cash bonuses under Scheme I.

For Scheme II, the incremental compensation expense varies depending on 7Road’s financial performance. In the third quarter of 2013, 7Road granted to an additional 48 7Road employees the right to receive an annual cash bonus under Scheme II with the same terms as described above. For the year ended December 31, 2013, compensation expense of \$0.4 million was recognized in the consolidated statements of comprehensive income.

***Taxation***

Under the current laws of the Cayman Islands, we are not subject to tax on income or capital gains. In addition, payment of dividends by us is not subject to withholding tax in the Cayman Islands.

Under the current Hong Kong Inland Revenue Ordinance, entities incorporated in Hong Kong are subject to 16.5% profit tax on their taxable income generated from operations in Hong Kong.

***PRC Corporate Income Tax***

On January 1, 2008, the CIT Law, which unifies the statutory income tax rate of enterprises in China to generally 25%, became effective. The CIT Law provides a up to five-year transitional period from years 2008 to 2012 for those enterprises which enjoyed a favorable income tax rate of less than 25% under the Previous Income Tax Laws and Rules and were established before March 16, 2007, to gradually raise their rates to 25%.



On April 14, 2008, relevant governmental regulatory authorities released qualification criteria, application procedures and assessment processes for NHTEs which will be entitled to a favorable statutory tax rate of 15%. On July 8, 2008, relevant governmental regulatory authorities further clarified that NHTEs previously qualified under the Previous Income Tax Laws and Rules as of December 31, 2007 could retain their previous status as an NHTe, and could enjoy a preferential tax rate under the CIT Law, on condition that they were re-approved for NHTe status under new regulations released on April 14, 2008 and on July 8, 2008. Both AmazGame and Gamease were approved as NHTEs, and each of them is therefore eligible for the preferential tax rate under the CIT Law. For the years ended December 31, 2012 and 2013, AmazGame and Gamease were entitled to a tax rate of 15%. In order to continue to enjoy the preferential tax rate applicable to NHTEs, both AmazGame and Gamease will be required to renew their NHTe status every three years and make record filings with the local tax bureau. Moreover, Gamespace qualified as a software enterprise and enjoyed an income tax exemption for the 2012 and 2013 fiscal years and will be entitled to a 50% tax reduction to a rate of 12.5% for the subsequent three years.

Pursuant to a circular issued by the Ministry of Finance of the PRC and the State Administration of Taxation of the PRC on February 22, 2008, AmazGame and Gamease qualified as software enterprises which were subject to a 50% tax reduction to a rate of 12.5% for the 2011 fiscal year. Shenzhen 7Road qualified as a software enterprise in 2009 and enjoyed a 50% tax reduction to a rate of 12.5% for the fiscal years 2011 through 2013. Shanghai ICE qualified as a software enterprise and enjoyed an income tax exemption for the 2011 fiscal year and was entitled, and will be entitled, to 50% tax reduction to a rate of 12.5% for the subsequent three years. ICE Information and 7Road Technology qualified as software enterprises entitled to an income tax exemption for two years beginning with their first profitable year and a 50% tax reduction for the subsequent three years, if they continue to maintain the qualifications. 7Road Technology was profitable in 2013 and enjoyed an income tax exemption for that year.

In addition, AmazGame qualified as a “Key National Software Enterprise” for 2013 and 2014, which entitles it to a further reduced preferential tax rate of 10% for those years, subject to approval of the relevant tax authority.

We are subject to withholding taxes on the initial license fees and ongoing revenue-based royalties received from our licensees in various jurisdictions outside of the PRC. We recognize such foreign withholding taxes as income tax expense when related revenue of initial license fees and ongoing revenue-based royalties are recognized. Income tax expense related to such withholding taxes was \$2.1 million, \$1.7 million and \$1.5 million, respectively for the years ended December 31, 2013, 2012 and 2011.

Under the CIT Law and its implementation rules, the profits of a foreign invested enterprise arising in 2008 and onwards which are distributed to its immediate holding company outside the PRC will be subject to a withholding tax rate of 10%. A lower withholding tax rate will be applied if there is a tax treaty between the PRC and the jurisdiction of the foreign holding company. Holding companies in Hong Kong, for example, will be subject to a 5% withholding tax rate under the China-HK Tax Arrangement if such holding companies are considered non-PRC resident enterprises, and hold at least 25% of the equity interests in the foreign invested enterprises distributing the dividends, subject to approval of the PRC local tax authority. However, if the Hong Kong resident enterprise is not considered to be the beneficial owner of such dividends under applicable PRC tax regulations, such dividend may remain subject to withholding tax rate of 10%.

On April 1, 2009, AmazGame declared a dividend to Changyou HK, its immediate parent company in Hong Kong. We accrued a withholding tax of \$5.0 million based on the 5% withholding tax rate. Such \$5.0 million withholding tax was paid in the third quarter of 2009, based on the approval of the PRC local tax authority.

On October 27, 2009, the SAT issued Circular 601, which provides guidance on determining whether an enterprise is a beneficial owner under China’s tax treaties and tax arrangements. If any of our Hong Kong subsidiaries is, in the light of Circular 601, considered to be a non-beneficial owner for purposes of the China-HK Tax Arrangement, any dividends paid to it by any of our PRC subsidiaries would not qualify for the preferential dividend withholding tax rate of 5%, but rather would be subject to the usual CIT Law rate of 10%.

Our Board of Directors decided to cause one of our PRC subsidiaries to distribute 100% and 50% of its earnings for the year ended December 31, 2012 and 2013, respectively, of its earnings to its overseas parent company, Changyou HK. Based on an assessment performed pursuant to requirements specified by PRC tax authorities, our management concluded that such distribution would be subject to a 5% withholding tax, and we accrued deferred tax liabilities in the amount \$11.9 million and \$6.9 million, respectively, for 2012 and 2013 for withholding taxes associated with this distribution plan.

We do not intend to cause any of our PRC subsidiaries to distribute any profits of such subsidiaries with respect to the years prior to 2014 to their direct overseas parent companies, but rather intend that such profits will be retained by such subsidiaries for their PRC operations.



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*Transition from PRC Business Tax to PRC Value Added Tax*

The Pilot Program for transition from the imposition of Business Tax to the imposition of VAT for revenues from certain industries was launched in Shanghai on January 1, 2012. Beginning on September 1, 2012, the Pilot Program was expanded from Shanghai to eight other cities and provinces in China, including Beijing.

Cinema advertising revenues became subject to VAT on January 1, 2012 and online advertising revenues became subject to VAT on September 1, 2012, each at a rate of 6%. Effective December 1, 2012, revenues derived from Web game operations that were not developed in house became subject to VAT at a rate of 6%.

*Business Tax and related Surcharges*

Prior to the Pilot Program, the Changyou group was subject to a 5% Business Tax and 0.6% related surcharges on revenues from MMOG operations, our online advertising business in the PRC, and our cinema advertising business in the PRC. Business Tax and the related surcharges are recognized when the revenue is earned.

After the Pilot Program, revenues generated from our MMOG operations continue to be subject to Business Tax and related surcharges.

*VAT*

Prior to the Pilot Program, in addition to Business Tax and related surcharges, we were subject to VAT at an effective rate of 3% for the revenues from inter-company software sales in the PRC.

In 2011, with the consolidation of 7Road, VAT has been imposed on our in-house developed Web game revenues at a rate of 17%, with a 14% immediate tax refund, resulting in a net rate of 3%, plus a related surcharge of 2% on such revenues.

After the Pilot Program, our online advertising and cinema advertising revenues are now also subject to VAT at a rate of 6%.

There is an additional culture construction fee surcharge of 3% on revenues from our online advertising and cinema advertising businesses. In addition, our entities incorporated in Beijing were subject to a surcharge at the rate of 0.72% on their revenues for the year ended December 31, 2013.

*Critical Accounting Policies and Estimates*

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States, appearing elsewhere in this annual report. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, mezzanine equity, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We have identified below the accounting policies that reflect our more significant estimates and judgments, and those that we believe are the most critical to fully understanding and evaluating our consolidated financial statements.

When reviewing our financial statements, you should consider (i) our selection of critical accounting policies, (ii) the judgment and other uncertainties affecting the application of such policies and (iii) the sensitivity of reported results to changes in conditions and assumptions.

*Basis of Presentation and Consolidation*

Our consolidated financial statements have been prepared on a historical cost basis to reflect our financial position and results of operations in accordance with U.S. GAAP and on a going concern basis.



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The consolidated financial statements include the financial statements of Changyou.com Limited and its controlled operating entities, including subsidiaries and VIEs. All inter-company balances and transactions within the Changyou group have been eliminated on consolidation.

We have adopted the guidance of accounting for VIEs, which requires VIEs to be consolidated by the primary beneficiary of the entity. Our management made evaluations of the relationships between us and our VIEs and the economic benefit flow of contractual arrangements with the VIEs. In connection with such evaluation, management also took into account the fact that, as a result of such contractual arrangements, we control the shareholders' voting interests in the VIEs. As a result of such evaluation, management concluded that Changyou.com Limited, through its indirect PRC subsidiaries, is the primary beneficiary of its VIEs. As a result, we consolidate all of our VIEs in our consolidated financial statements.

Because we and the 17173 Business are under common control by Sohu, in accordance with ASC subtopic 805-50 our consolidated financial statements for the year ended December 31, 2011 were prepared as if the current corporate structure had been in existence throughout the periods presented.

Certain acquired assets of the combining entities and businesses were combined using the existing book values from the perspective of Sohu, the controlling party. No amount was recognized in consideration of goodwill or for the excess of our interest in the net fair value of the 17173 Business's identifiable assets, liabilities and contingent liabilities over cost at the time of the common control combination, to the extent of the continuation of Sohu's interest.

ASC subtopic 805-50 provides that consolidated statements of comprehensive income should include the results of each of the combining entities and businesses from the earliest date presented or, if more recent, from the date when the combining entities and businesses first came under common control, regardless of the date of the common control combination.

#### *Online Game Revenues*

##### *MMOG operations*

We earn revenue through providing MMOGs to players pursuant to the item-based revenue model. Under the item-based model, the basic game play functions are free of charge and players are charged for purchases of in-game virtual items.

Game operations revenues are collected by our VIEs through the sale of our prepaid cards, which we sell in both virtual and physical forms to third-party distributors and players. Proceeds received from sales of prepaid cards are initially recorded as receipts in advance from customers and, upon activation or charge of the prepaid cards, are transferred from receipts in advance from customers to deferred revenues. As we do not have control of, and generally do not know, the ultimate selling price of the prepaid cards sold by distributors, net proceeds from distributors form the basis of revenue recognition.

Under the item-based revenue model, revenue is recognized over the estimated lives of the virtual items purchased or as the virtual items are consumed. If different assumptions were used in deriving the estimated lives of the virtual items, the timing in which we record our revenues would be impacted.

Revenues are recorded net of business tax, discounts and rebates to distributors.

Prepaid cards will expire two years after the date of card production if they have never been activated. The proceeds from the expired game cards are recognized as revenue upon expiration of cards.

Once the prepaid cards are activated and credited to a player's personal game account, they will not expire as long as the personal game account remains active. We are entitled to suspend and close a player's personal game account if it has been inactive for a period of 180 consecutive days. The unused balances in an inactive player's personal game account are recognized as revenues when the account is suspended and closed.

For the years ended December 2013, 2012 and 2011, we recognized revenues in connection with expired un-activated prepaid cards and unused balances in inactive accounts of approximately \$951,000, \$627,000 and \$964,000, respectively.





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## Web games

See “—Revenue Recognition—Web games”.

## Overseas licensing

We enter into licensing arrangements with overseas licensees to operate our MMOGs in other countries or administrative regions. These licensing agreements provide two revenue streams, consisting of an initial license fee and a monthly revenue-based royalty fee based on monthly revenue and sales from ancillary products of the games. The initial license fee is based on both a fixed amount and additional amounts receivable upon the game's achieving certain sales targets. Since we are obligated to provide post-sales services such as technical support and provision of updates and when-and-if-available upgrades to the licensees during the license period, the initial license fee from the licensing arrangement is recognized as revenue ratably over the license period. The fixed amount of the initial license fee is recognized ratably over the remaining license period from the launch of the game and the additional amount is recognized ratably over the remaining license period from the date such additional amount is certain. The monthly revenue-based royalty fee is recognized when relevant services are delivered, provided that collectability is reasonably assured.

## Online Advertising Revenues

Our online advertising revenues are generated from the 17173 Business. A contract is signed to establish a fixed price and the advertising services to be provided. Based on the contracts, the 17173 Business provides advertisement placements on its Websites and/or in different formats, including, among other things, banners, links, logos, buttons, rich media and content integration.

To determine the method of recognition of online advertising revenue, prior to entering into contracts, management makes a credit assessment of the customer to assess the collectability of the contract. For those contracts for which collectability is determined to be reasonably assured, revenue is recognized ratably over the period during which the advertising services are provided and when all revenue recognition criteria are met. For those contracts for which collectability is determined to not be reasonably assured, revenue is recognized only when the cash is received and all other revenue recognition criteria are met.

Before 2011, the 17173 Business treated multiple deliverable elements of advertising contracts as a single unit of accounting for revenue recognition purposes. On January 1, 2011, in accordance with ASU No.2009 -13, the 17173 Business began to treat advertising contracts with multiple deliverable elements as separate units of accounting for revenue recognition purposes and to recognize revenue on a periodic basis during the contract periods when each deliverable service was provided. Since the contract price is for all the deliverables under an advertising contract, the 17173 Business allocates the contract price among all the deliverables at the inception of the arrangement on the basis of their relative selling prices according to the selling price hierarchy established by ASU No.2009 -13. The 17173 Business first uses vendor-specific objective evidence of selling price, if it exists. If vendor-specific objective evidence of selling price does not exist, the 17173 Business uses third-party evidence of selling price. If neither vendor-specific objective evidence of selling price nor third-party evidence of selling price exists, the 17173 Business uses management's best estimate of the selling price for the deliverable.

The Pilot Program for transition from the imposition of Business Tax to the imposition of VAT for revenues from certain industries was launched in Shanghai on January 1, 2012. On September 1, 2012, the Pilot Program was expanded from Shanghai to eight other cities and provinces in China, including Beijing. Our online advertising revenues became subject to the Pilot Program on September 1, 2012 and are now subject to VAT, instead of Business Tax, at a rate of 6%. Online advertising revenues are recognized after deducting agent rebates and net of VAT and related surcharges.

## IVAS Revenues

We offer Web games developed by third-party developers and generate revenues from the provision of IVAS, including promotion, access maintenance and payment services, to third-party developers. Under revenue-sharing agreements that we sign with third-party developers, we collect payments from the end users, keep a pre-agreed percentage of the proceeds and remit the balance to the third-party developers. Revenues from IVAS are recognized when our obligations under the agreements and all other revenue recognition criteria have been met. Revenues from IVAS are recognized under the gross method as we are the principal obligor with respect to provision of the services

## Others Revenues

For cinema advertising revenues, a contract is signed with the advertiser to establish a fixed price and specify advertising services to be provided. Based on the contracts, we provide advertisement placements in advertising slots to be shown in theatres before the screening of movies. Revenue from cinema advertising is recognized when all the recognition criteria are met. Depending



on the terms of a customer contract, fees for services performed can be recognized according to two principal methods, consisting of the proportional performance method and the straight-line method. Under the proportional performance method, fees are generally recognized based on a percentage of the advertising slots actually delivered where the fee is earned on a per-advertising slot placement basis. Under the straight-line method, fees are recognized on a straight-line basis over the contract period when the fee is not paid based on the number of advertising slots actually delivered.



### *Presentation of PRC Value Added Tax and Business Tax*

Under ASC 605-45, the presentation of taxes on either a gross basis (included in revenues and costs) or a net basis (excluded from revenues) is an accounting policy decision determined by management.

As VAT imposed on online advertising and cinema advertising revenues and VAT imposed on 7Road's revenues deemed to be from the sale of software are considered as substantially different in nature, we determined that it is reasonable to apply the guidance separately for these two types of VAT. VAT payable on online advertising and cinema advertising revenues is the difference between the output VAT (at a rate of 6%) and available input VAT amount (at the rate applicable to the supplier) which is the VAT paid to suppliers in relation to the cost for provision of online advertising and cinema advertising services. On the other hand, VAT is payable by 7Road at an effective rate of 3% of revenues deemed to be from the sale of software, irrespective of the availability of any input VAT, under preferential VAT treatment provided to 7Road by the local tax bureau.

We adopted the net presentation method for our MMOG revenues, online advertising revenues and cinema advertising revenues and adopted the gross presentation method for the revenues of 7Road deemed to be derived from the sale of software.

Under the net presentation method, the revenues were net of business tax (at a rate of 5%) or value added tax (at a rate of 6%), as applicable.

Under the gross presentation method, we present PRC VAT on a gross basis, by which VAT collected from customers at a rate of 17% is included in revenues, and the net VAT payment at the effective PRC VAT rate of 3% is included in cost of revenues, because we consider 7Road's 17% VAT obligation and its entitlement to a 14% VAT refund as one integrated preferential VAT policy.

### *Share-Based Compensation Expenses*

Share-based compensation expense is for share awards, including ordinary shares, share options, restricted shares and restricted share units, granted by us to our employees, directors and certain Sohu employees. Share-based compensation expense is recognized as costs and/or expenses in the financial statements based on the fair values of the related share-based awards on their grant dates.

In determining the fair value of our ordinary shares, restricted shares and restricted share units granted in January and April 2008, the income approach/discounted cash flow method with a discount for lack of marketability is applied given that the shares underlying the awards were not publicly traded at the time of the grant.

Determining the fair value of ordinary shares requires complex and subjective judgments regarding our projected financial and operating results, our unique business risks, the liquidity of our ordinary shares and our operating history and prospects at the time of the grants.

Because at the time of the grants our business was at a different stage of its product life cycle than that of the publicly listed companies in the online game industry, it was concluded that a market comparison approach would not have been meaningful in determining the fair value of our ordinary shares. As a result, we used the income approach/discounted cash flow method to derive the fair values. We applied the discounted cash flow, or DCF, analysis based on our projected cash flow using management's best estimate as of the respective valuation dates. The projected cash flow estimate included, among other things, an analysis of projected revenue growth, gross margins, effective tax rates, capital expenditures and working capital requirements. The income approach involves applying appropriate discount rates, based on earnings forecasts, to estimated cash flows. The assumptions we used in deriving the fair value of our ordinary shares were consistent with the assumptions used in developing our MMORPG business plan, which included no material changes in the existing political, legal, fiscal and economic conditions in China; our ability to recruit and retain competent management, key personnel and technical staff to support our ongoing operations; and no material deviation in industry trends and market conditions from economic forecasts. These assumptions are inherently uncertain and subjective. The discount rates reflect the risks the management perceived as being associated with achieving the forecasts and are based on our estimated cost of capital, which was derived by using the capital asset pricing model, after taking into account systemic risks and company-specific risks. The capital asset pricing model is a model for pricing securities that adds an assumed risk premium rate of return to an assumed risk-free rate of return. Using this method, we determined the appropriate discount rates to be 22% as of the January 2008 valuation date and 23% as of the April 2008 valuation date.



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We also applied a discount for lack of marketability, or DLOM, to reflect the fact that, at the time of the grants, we were a closely-held company and there was no public market for our ordinary shares. To determine the discount for lack of marketability, we used the Black-Scholes option pricing model. Pursuant to the Black-Scholes option pricing model, we used the cost of a put option, which can be used to hedge the price change before a privately held share can be sold, as the basis to determine the discount for lack of marketability. Based on the foregoing analysis, we used a DLOM of 19% to discount the value of our ordinary shares as of the January 2008 and April 2008 valuation dates.

Because there was no evidence to indicate that there would be a disproportionate return between majority and minority shareholders, we did not apply a minority discount. As a result, it was concluded that our fair value as a going concern was \$136 million as of the January 2008 valuation date and \$198 million as of the April 2008 valuation date.

In determining the fair value of our restricted share units granted in 2009 before our initial public offering, the fair value of the underlying shares was determined based on the offering price of ADSs in the offering. In determining the fair value of restricted share units granted after the initial public offering, the fair value was determined based on the market price of our ADSs on the grant dates.

In determining the fair value of share options granted by Sohu to our employees, we applied the Black-Scholes valuation model. Restricted share units granted by Sohu to our employees were measured based on the fair market value of the underlying stock on the dates of grants.

Share-based compensation expense for ordinary shares granted is fully recognized in the quarter during which these ordinary shares are granted. Share-based compensation expense for share options, restricted shares and restricted share units granted is recognized on an accelerated basis over the requisite service period. The number of share-based awards for which the service is not expected to be rendered over the requisite period is estimated, and the related compensation expense is not recorded for that number of awards.

The assumptions used in share-based compensation expense recognition represent management's best estimates based on historical experience and consideration to developing expectations about the future. These estimates involve inherent uncertainties and the application of management judgment, however. If factors change or different assumptions are used, the share-based compensation expense could be materially different for any period. Moreover, the estimates of fair value are not intended to predict actual future events or the value that ultimately will be realized by employees who receive equity awards, and subsequent events are not indicative of the reasonableness of the original estimates of fair value made by us for accounting purposes.

For the years ended December 31, 2013, 2012 and 2011, our share-based compensation expenses amounted to \$1.3 million, \$3.7 million and \$6.1 million, respectively.

We have used a retrospective valuation for the determination of fair value of ordinary shares and RSUs granted by 7Road.com Limited, or 7Road, to its employees. We used the discounted cash flow, or DCF, method of the income approach to derive the fair value of 7Road's ordinary shares. The determination of the fair value of 7Road's ordinary shares required complex and subjective judgments to be made regarding its projected financial and operating results, its unique business risks, the liquidity of its shares and its operating history and prospects at the time of valuation. The income approach involves applying an appropriate discount rate to estimated cash flows that are based on earnings forecasts developed by 7Road. The assumptions used in deriving the forecasts were consistent with 7Road's business plan.

Under the 7Road 2012 Share Incentive Plan, 2,546,250 restricted share units had been granted as of December 31, 2012. Such restricted share units were not to be vested until 7Road's completion of a firm commitment underwritten IPO of its shares resulting in a listing on an internationally recognized exchange and the expiration of all underwriters' lockup periods applicable to the IPO. An IPO event is not considered to be probable until it is completed. Under ASC 718, compensation cost should not be accrued if it is not probable that the performance condition will be achieved. As a result, no share-based compensation expense relating to these restricted share units was recognized for the year ended December 31, 2012.

On June 28, 2013, 7Road's Board of Directors approved the cancellation of the 7Road 2012 Share Incentive Plan. See "—Operating Expenses—Share-based Compensation Expenses—7Road share-based awards."



### *Determination of the Fair Value of Contingent Consideration*

The acquisition of 7Road includes a contingent consideration arrangement that requires additional consideration to be paid by us based on the future financial performance of 7Road through December 31, 2012. The range of the undiscounted amounts we could pay under the contingent consideration agreement is between \$nil and \$32.76 million. The fair value of the contingent consideration of \$28.05 million recognized on the acquisition date was estimated using the income approach. There were no indemnification assets involved. Based on 7Road's performance having exceeded the milestone level for the year ended December 31, 2012, we recorded a change in fair value of the contingent consideration of \$2.2 million in other expense.

The contingent consideration as at December 31, 2013 represents the fair value of potential payments under the contingent consideration arrangement for our acquisition of Doyo. The contingent consideration arrangement requires additional consideration to be paid by us based on the achievement by Doyo of specified performance milestones for the years 2013 to 2015. The fair value of the contingent consideration was recognized on the date of the acquisition, with the income approach applied.

The acquisition of the RaidCall Business includes a contingent consideration arrangement that gives us the right to acquire additional shares of TalkTalk if specified conditions occur through the 2014 fiscal year. The range of the additional shares of TalkTalk that we could acquire under this arrangement is between nil and 7.5% of the outstanding shares on a post-issuance, fully-diluted basis. The fair value of the contingent consideration of \$nil was recognized on the acquisition date, as our management determined that it is unlikely that the specified conditions will occur.

### *Mezzanine Equity*

On May 11, 2011, we, through Gamease, acquired 68.258% of the equity interests in 7Road and began to consolidate 7Road's financial statements on June 1, 2011.

Mezzanine equity consists of non-controlling interest in 7Road and a put option pursuant to which the non-controlling shareholders will have the right to put their equity interests in 7Road to us at a pre-determined price if 7Road achieves specified performance milestones before the expiry of the put option and 7Road does not complete an initial public offering on NASDAQ, the New York Stock Exchange or the Stock Exchange of Hong Kong. The put option will expire in 2014. Since the occurrence of the put is not solely within our control, we classify the non-controlling interest as mezzanine equity instead of permanent equity in our consolidated financial statements.

In accordance with ASC subtopic 480-10, we calculate, on an accumulative basis from the acquisition date, (i) the amount of accretion that would increase the balance of non-controlling interest to its estimated redemption value over the period from the date of the 7Road acquisition to the earliest redemption date of the non-controlling interest and (ii) the amount of net profit attributable to non-controlling shareholders of 7Road based on their ownership percentage. The carrying value of the non-controlling interest as mezzanine equity will be adjusted by an accumulative amount equal to the higher of (i) and (ii).

On May 1, 2013, we entered into an agreement to acquire all of the ordinary shares of 7Road held by the non-controlling shareholders. The acquisition closed on June 5, 2013. Under ASC 810-10, changes in a parent's ownership interest while the parent retains control of its subsidiary are accounted for as equity transactions, and do not impact net income or comprehensive income in the consolidated financial statements. Following the closing of the acquisition, \$2.4 million, representing the excess of the amount of the mezzanine-classified non-controlling interest in 7Road over the purchase price as of the closing date, was recorded in our equity accounts.

For the year ended December 31, 2013, accretion charges of \$17.8 million, compared to \$11.2 million and \$2.6 million, respectively, for the years ended December 31, 2012 and 2011, were recorded in our statements of comprehensive income as net income attributable to the mezzanine-classified non-controlling interest shareholders of 7Road.

### *Treasury Shares*

On July 27, 2013, our Board of Directors authorized a share repurchase program of up to \$100 million over a two-year period from July 27, 2013 to July 26, 2015. The timing and actual number of shares subject to repurchase are at the discretion of our management and contingent on market conditions and share prices, among other factors.

We account for repurchased ordinary shares under the cost method and include such repurchase ordinary shares in treasury shares as an offsetting component of the shareholders' equity. Cancellation of treasury shares, if it incurs in the future, would be recorded as a reduction of ordinary shares and additional paid in capital/retained earnings, as applicable. In case of reissuance of treasury shares, the difference between the cost of treasury shares and cash received would be charged into additional paid in capital/retained earnings, as applicable.





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As of December 31, 2013, we had repurchased 590,500 ADSs (equivalent to 1,181,000 Class A ordinary shares), which were recorded as treasury shares pending cancellation, for a total repurchase price amounting to approximately \$17.3 million pursuant to the referenced share repurchase program.

#### *Determination of Segment Aggregation*

Operating segments are defined as components of an enterprise about which separate financial information is available and is evaluated regularly by the chief operating decision maker, or the CODM, or a decision making group, in deciding how to allocate resources and in assessing performance. Our CODM is our chief executive officer.

Before 2011, we principally engaged in the development, operation and licensing of MMOGs and operated and managed this business as a single segment. In 2011, we expanded our business by acquisitions in the Web game, online advertising and cinema advertising businesses, and generated revenues from the operations of such businesses. With the goal of optimizing the management of operations, our CODM separately reviewed key information of each of four operating segments, consisting of MMOG, Web game, online advertising and cinema advertising. We concluded that the MMOG and Web game segments have similar economic characteristics and meet all of the aggregation criteria that are required under ASC280 to aggregate identified operating segments. Hence we aggregated the MMOG and Web game segments as one reportable segment under online game.

#### *Determination of Allowance of Doubtful Accounts*

The carrying value of accounts receivable is reduced by an allowance that reflects our best estimate of the amounts that will not be collected. We make estimations of the collectability of accounts receivable. Many factors are considered in estimating the general allowance, including but not limited to reviewing delinquent accounts receivable, performing aging analyses and customer credit analyses, and analyzing historical bad debt records and current economic trends. Additional allowance for specific doubtful accounts might be made if our customers are unable to make payments due to their deteriorating financial conditions.

#### *Income Tax and Valuation Allowance Against Deferred Tax Assets*

We estimate income tax expense for each jurisdiction in which we operate and for each period presented, which includes estimating current tax exposure as well as assessing realizable deferred tax assets and deferred tax liabilities.

As of December 31, 2013, our deferred tax assets mainly comprised temporary differences arising from (1) net operating losses; (2) accrued but unpaid salaries and bonuses; and (3) the book and tax bases of intangible assets. We recorded an allowance against gross deferred tax assets based on uncertainty over the profitability of related subsidiaries and over whether temporary differences can be claimed. If events were to occur in the future that would allow us to realize more of our deferred tax assets than the presently recorded amount, an adjustment would be made to the deferred tax assets that would increase income for the period. If events were to occur in the future that would require us to realize less of our deferred tax assets than the presently recorded amount, an adjustment would be made to the valuation allowance against deferred tax assets that would decrease income for the period. Significant management judgment is required in determining income tax expense and deferred tax assets and liabilities. As of December 31, 2013 and 2012, our net deferred tax assets were \$5.7 million and \$5.0 million, respectively, resulting from temporary differences between accounting and tax bases.

#### *Assessment of Impairment for Long-lived Assets, Equity Investments and Goodwill*

Our long-lived assets include intangible assets, fixed assets and other assets.

Intangible assets mainly comprise definite-lived intangible assets, including operating rights of licensed games, computer software purchased from unrelated third parties, developed technologies and cinema advertising slot rights, and indefinite-lived intangible assets, including trade names, which are separable from fixed assets. We amortize the cost of intangible assets over their expected future economic lives. Fixed assets mainly comprise office building, computer equipment (including servers) and leasehold improvements, and are depreciated over the estimated useful lives of the assets on a straight-line basis. Other assets mainly represent long-term loans to employees, accrued interest income and long-term deposits. Management's judgment is required in the assessment of the economic lives of intangible assets and useful lives of the fixed assets and other assets. Based on the existence of one or more indicators of impairment, we measure any impairment of intangible assets, fixed assets and other assets based on a projected discounted cash flow method using a discount rate determined by our management which is commensurate with the risk inherent in our business model. An impairment charge would be recorded if we determined that the carrying value of intangible assets, fixed assets or other assets may not be recoverable. Our estimates of future cash flows require significant judgment based on our historical results and anticipated results and are subject to many factors. As of December 31, 2013, 2012 and 2011, our impairment charges for intangible assets were \$17.2 million, \$12.4 million and \$3.8 million, respectively.



We continually review our investments in an investee to determine whether a decline in fair value below the carrying value is other than temporary. The primary factors we consider in our determination are the length of time that the fair value of the investment is below its carrying value; and the financial condition, operating performance and near-term prospects of the investee. The determination of whether a decline in value is other than temporary requires significant judgment. If the decline in fair value is deemed to be other than temporary, the carrying value of the investment is written down to fair value. Write-downs for equity method investments are included in equity in losses of affiliated companies. For the years ended December 31, 2013, 2012 and 2011, our impairment losses for equity investments were \$0.9 million, \$nil and \$0.6 million, respectively.

Goodwill represents the excess of the purchase price over the fair value of the identifiable assets and liabilities acquired as a result of our acquisitions of interests in our subsidiaries and VIEs.

We test goodwill for impairment at the reporting unit level on an annual basis as of October 1, and between annual tests when an event occurs or circumstances change that could indicate that the asset might be impaired. Commencing in September 2011, in accordance with the FASB revised guidance on "Testing of Goodwill for Impairment," a company first has the option to assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the company decides, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is mandatory. Otherwise, no further testing is required. The quantitative impairment test consists of a comparison of the fair value of goodwill with its carrying value. Application of a goodwill impairment test requires significant management judgment, including the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units, and determining the fair value of each reporting unit. The judgment in estimating the fair value of reporting units includes estimating future cash flows, determining appropriate discount rates and making other assumptions. Changes in these estimates and assumptions could materially affect the determination of fair value for each reporting unit.

If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss should be recognized in an amount equal to that excess. The goodwill impairment losses for the years ended December 31, 2013, 2012 and 2011 were \$nil, \$nil and \$5.2 million, respectively.

#### *Short-term Investments*

In accordance with ASC 825, for investments in financial instruments with a variable interest rate indexed to the performance of underlying assets, we elected the fair value method at the date of initial recognition and carried these investments subsequently at fair value. Changes in the fair value are reflected in our consolidated statements of comprehensive income. To estimate fair value, we refer to the quoted rate of return provided by banks at the end of each period using discounted cash flow method. We classify the valuation techniques that use these inputs as Level 2 of fair value measurement. Since these investments' maturity dates are within one year, they are classified as short-term investments. For the years ended December 31, 2013, 2012 and 2011, we recorded changes in the fair value of short-term investments in our consolidated statements of comprehensive income of \$2.5 million, \$1.5 million and \$659,000, respectively.

#### *Determination of Functional Currencies*

Our reporting and functional currency is the U.S. dollar. The functional currency of our subsidiaries and our VIEs in China is the RMB. The functional currency of our subsidiary in the United Kingdom is the British Pound, the functional currency of our subsidiary in Malaysia is the Malaysian Ringgit, the functional currency of our subsidiary in Korea is the Korean Won, the functional currency of our subsidiaries in Hong Kong and the United States of America is the U.S. dollar. An entity's functional currency is the currency of the primary economic environment in which it operates. Normally, that is the currency of the environment in which it primarily generates and expends cash. Management's judgment is essential in the determination of the functional currency which is made by assessing various indicators, such as cash flows, sales price and market, expenses, financing and inter-company transactions and arrangements. Assets and liabilities of our subsidiaries and VIEs in China are translated into U.S. dollars, our reporting currency, at the exchange rate in effect at the balance sheet date and revenues and expenses are translated at the current exchange rate in effect during the reporting period. Foreign currency translation adjustments are not included in determining net income for the period but are accumulated in a separate component of consolidated equity on the balance sheet. The accumulated foreign currency translation adjustment as of December 31, 2013, 2012 and 2011 was a gain of \$71.7 million, \$38.1 million and \$34.7 million, respectively.

**Year to Year Comparisons***Year Ended December 31, 2013 Compared to Year Ended December 31, 2012*

**Revenues.** Total revenues for the year ended December 31, 2013 increased by \$114.5 million to \$737.9 million, compared to \$623.4 million for the year ended December 31, 2012.

Online game revenues for the year ended December 31, 2013 increased by \$98.9 million to \$669.2 million, compared to \$570.3 million year for the year ended December 31, 2012. The increase was mainly due to increased revenues from TLBB and the growth of Wartune overseas revenues in 2013.

Online advertising revenues, which consist of revenues generated from the 17173 Business, for the year ended December 31, 2013 increased by \$7.5 million to \$50.0 million, compared to \$42.5 million for the year ended December 31, 2012. The increase was mainly due to an increase in advertising rates of the 17173.com Website and improved advertising sales in 2013.

IVAS revenues, which consist of revenues generated from the operation of third-party Web games by the 17173 Business, for the year ended December 31, 2013 increased by \$1.1 million to \$5.4 million, compared to \$4.3 million for the year ended December 31, 2012. The increase was mainly due to more Web games and a larger number of users playing Web games operated by the 17173 Business in 2013.

Others revenues, which consist of cinema advertising revenues, for the year ended December 31, 2013 increased by \$7.0 million to \$13.3 million, compared to \$6.3 million for the year ended December 31, 2012. The increase was mainly due to increased advertising sales in 2013 due to improvements in the sales function.

**Cost of Revenues.** Our cost of revenues increased by \$21.9 million to \$126.4 million for the year ended December 31, 2013, compared to \$104.5 million for the year ended December 31, 2012. The increase was primarily due to an increase in our salary and benefits expenses, which increased by \$9.5 million to \$38.1 million for the year ended December 31, 2013, compared to \$28.6 million for the year ended December 31, 2012, our revenue-based royalty payments to game developers, which increased by \$3.1 million to \$9.4 million for the year ended December 31, 2013, compared to \$6.3 million for the year ended December 31, 2012, our Business Tax and VAT cost, which increased by \$4.4 million to \$8.9 million for the year ended December 31, 2013, compared to \$4.5 million for the period for the year ended December 31, 2012, our content and license costs, which increased by \$2.3 million to \$4.7 million, compared to \$2.4 million for the year ended December 31, 2012 and our bandwidth leasing and communication costs, which increased by \$1.6 million to \$19.5 million for the year ended December 31, 2013, compared to \$17.9 million for the year ended December 31, 2012. In addition, we incurred costs of \$17.5 million for our cinema advertising business for the year ended December 31, 2013, compared to \$20.0 million for the year ended December 31, 2012.

**Gross Profit.** As a result of the foregoing, our gross profit increased by \$92.5 million to \$611.4 million for the year ended December 31, 2013, compared to \$518.9 million for the year ended December 31, 2012. Our gross margin was 82.9% and 83.2%, respectively, for the years ended December 31, 2013 and December 31, 2012. The decrease in gross margin was mainly due to an increase in salaries and benefits, higher bandwidth costs incurred and higher expenses related to licensed games in 2013.

**Operating Expenses**

- **Product Development Expenses.** Product development expenses increased by \$46.1 million to \$119.9 million for the year ended December 31, 2013, compared to \$73.8 million for the year ended December 31, 2012. The increase was primarily because salary and benefits expense increased by \$32.0 million to \$87.7 million for the year ended December 31, 2013 compared to \$55.7 million for the year ended December 31, 2012, due to our hiring of more game engineers, content and license expenses increased by \$7.0 million to \$14.0 million for the year ended December 31, 2013, compared to \$7.0 million for the year ended December 31, 2012, facilities expenses increased by \$2.3 million to \$6.1 million for the year ended December 31, 2013, compared to \$3.8 million for the year ended December 31, 2012, and travel and entertainment expense increased by \$1.5 million to \$3.6 million for the year ended December 31, 2013, compared to \$2.1 million for the year ended December 31, 2012.



- **Sales and Marketing Expenses.** Sales and marketing expenses increased by \$68.2 million to \$128.8 million for the year ended December 31, 2013, compared to \$60.6 million for the year ended December 31, 2012. The increase was primarily due to an increase in advertising expense increased by \$59.3 million to \$101.6 million for the year ended December 31, 2013, compared to \$42.3 million for the year ended December 31, 2012 and salary and benefits increased by \$7.3 million to \$20.6 million for the year ended December 31, 2013 due to the hiring of more sales and marketing professionals, compared to \$13.3 million for the year ended December 31, 2012.
- **General and Administrative Expenses.** General and administrative expenses increased by \$23.7 million to \$57.2 million for the year ended December 31, 2013, compared to \$33.5 million for the year ended December 31, 2012. The increase was primarily due to increases in salary and benefits expense, which increased by \$13.3 million to \$30.8 million for the year ended December 31, 2013, compared to \$17.5 million for the year ended December 31, 2012 and professional expense, which increased by \$7.3 million to \$14.1 million for the year ended December 31, 2013, compared to \$6.8 million for the year ended December 31, 2012.
- **Goodwill Impairment and Impairment of Intangibles via Acquisitions of Businesses.** We did not incur any impairment loss for the year ended December 31, 2013.

**Operating Profit.** As a result of the foregoing, we had operating profit of \$305.5 million for the year ended December 31, 2013, compared to an operating profit of \$348.1 million for the year ended December 31, 2012.

**Interest Income.** For the year ended December 31, 2013 interest income was \$28.5 million, compared to \$15.9 million for the year ended December 31, 2012. The increase was primarily due to an increase in our average cash balance for the year and increases in interest rates.

**Foreign Currency Exchange Loss.** For the year ended December 31, 2013, foreign currency exchange loss was \$5.9 million, compared to \$0.6 million for the year ended December 31, 2012.

**Interest Expense.** For the year ended December 31, 2013, interest expense was \$8.8 million, compared to \$2.2 million for the year ended December 31, 2012. The increase was primarily due to an increase in the balance of the bank loans.

**Other Income/(Expenses).** For the year ended December 31, 2013, other income/(expense) represent other income of \$3.6 million, compared to other expense of \$ 0.2 million for the year ended December 31, 2012.

**Income Tax Expense.** Income tax expense was \$36.4 million for the year ended December 31, 2013, compared to \$67.4 million for the year ended December 31, 2012. The decrease was mainly due to the decrease of statutory income tax rate as our main operating subsidiary obtained a preferential tax rate of 10% for the year ended December 31, 2013, as compared to 15% for the year ended December 31, 2012.

**Net Income Attributable to Mezzanine Classified Non-controlling Interest.** In accordance with ASC subtopic 480-10, we calculate, on an accumulative basis from the acquisition date, (i) the amount of accretion that would increase the balance of non-controlling interest to its estimated redemption value over the period from the date of the 7Road acquisition to the earliest redemption date of the non-controlling interest and (ii) the amount of net profit attributable to non-controlling shareholders of 7Road based on their ownership percentage. The carrying value of the non-controlling interest as mezzanine equity will be adjusted by an accumulative amount equal to the higher of (i) and (ii). For the year ended December 31, 2013, the accretion charge was \$17.8 million, compared to \$11.2 million for the year ended December 31, 2012.

**Net Income Attributable to Changyou.com Limited.** As a result of the foregoing, we had net income attributable to Changyou.com Limited of \$268.6 million for the year ended December 31, 2013, compared to net income of \$282.4 million for the year ended December 31, 2012.

*Year Ended December 31, 2012 Compared to Year Ended December 31, 2011*

**Revenues.** Total revenues increased by \$138.8 million to \$623.4 million for the year ended December 31, 2012, compared to \$484.6 million for the year ended December 31, 2011. The increase was mainly due to the ongoing popularity of our flagship game TLBB and Wartune in China in 2012, a full year's revenue contribution from 7Road, and revenue growth of the 17173 Business.

**Cost of Revenues.** Our cost of revenues increased by \$37.0 million to \$104.5 million for the year ended December 31, 2012, compared to \$67.5 million for the year ended December 31, 2011. The increase was primarily due to an increase in our salary and benefits expenses, which increased by \$11.6 million to \$28.6 million for the year ended December 31, 2012, compared to \$17.0 million for the year ended December 31, 2011, our depreciation and amortization costs, which increased by \$6.6 million to \$14.8 million for the year ended December 31, 2012, compared to \$8.2 million for the year ended December 31, 2011, our bandwidth leasing and communication costs, which increased by \$5.5 million to \$17.9 million for the year ended December 31, 2012, compared to \$12.4 million for the year ended December 31, 2011, our revenue-based royalty payments to the game developers, which increased by \$2.3 million to \$6.3 million for the year ended December 31, 2012, compared to \$4.0 million for the year ended December 31, 2011, and 7Road's net PRC VAT, which increased by \$2.2 million to \$2.8 million for the year ended December 31, 2012, compared to \$0.6 million for the period between May 11, 2011 and December 31, 2011. In addition, we incurred costs of \$20.0 million for our cinema advertising business for the year ended December 31, 2012, compared to \$13.8 million for the year ended December 31, 2011.

**Gross Profit.** As a result of the foregoing, our gross profit increased by \$101.8 million to \$518.9 million for the year ended December 31, 2012, compared to \$417.1 million for the year ended December 31, 2011. Our gross margin was 83.2% and 86.1%, respectively, for the years ended December 31, 2012 and December 31, 2011. The decrease in gross margin was mainly due to an increase in salaries and benefits, an increase in depreciation and amortization costs, higher bandwidth costs incurred and higher expenses related to licensed games in 2012, as well as a higher negative gross margin from our cinema advertising business in 2012.

**Operating Expenses**

- **Product Development Expenses.** Product development expenses increased by \$21.6 million to \$73.8 million for the year ended December 31, 2012, compared to \$52.2 million for the year ended December 31, 2011. The increase was primarily because salary and benefits expense increased by \$16.9 million to \$55.7 million for the year ended December 31, 2012 compared to \$38.8 million for the year ended December 31, 2011, due to our hiring of more game engineers, content and license expenses increased by \$2.1 million to \$7.0 million for the year ended December 31, 2012, compared to \$4.9 million for the year ended December 31, 2011, facilities expenses increased by \$1.0 million to \$3.8 million for the year ended December 31, 2012, compared to \$2.8 million for the year ended December 31, 2011, and depreciation and amortization expense increased by \$1.0 million to \$4.0 million for the year ended December 31, 2012, compared to \$3.0 million for the year ended December 31, 2011.
- **Sales and Marketing Expenses.** Sales and marketing expenses increased by \$10.7 million to \$60.6 million for the year ended December 31, 2012, compared to \$49.9 million for the year ended December 31, 2011. The increase was primarily due to an increase in advertising expense increased by \$8.9 million to \$42.3 million for the year ended December 31, 2012, compared to \$33.4 million for the year ended December 31, 2011, salary and benefits increased by \$1.4 million to \$13.3 million for the year ended December 31, 2012 due to the hiring of more sales and marketing professionals, compared to \$11.9 million for the year ended December 31, 2011, and facilities expense increased by \$0.4 million to \$1.6 million for the year ended December 31, 2012, compared to \$1.2 million for the year ended December 31, 2011.





- **General and Administrative Expenses.** General and administrative expenses increased by \$3.8 million to \$33.5 million for the year ended December 31, 2012, compared to \$29.7 million for the year ended December 31, 2011. The increase was primarily due to increases in salary and benefits expense, which increased by \$2.6 million to \$17.5 million for the year ended December 31, 2012, compared to \$14.9 million for the year ended December 31, 2011, travelling and entertainment expense, which increased by \$0.8 million to \$2.2 million for the year ended December 31, 2012, compared to \$1.4 million for the year ended December 31, 2011, and professional expense, which increased by \$0.3 million to \$6.8 million for the year ended December 31, 2012, compared to \$6.5 million for the year ended December 31, 2011.
- **Goodwill Impairment and Impairment of Intangibles via Acquisitions of Businesses.** We incurred an impairment loss of \$2.9 million for the year ended December 31, 2012, which primarily comprised impairment of intangibles via acquisitions of businesses, which were fully impaired, compared to an impairment loss of \$5.4 million for the year ended December 31, 2011, which primarily comprised impairment of goodwill in the amount of \$5.2 million arising from our acquisition in the cinema advertising business, and impairment of an acquired trade name in the amount of \$0.2 million.

**Operating Profit.** As a result of the foregoing, we had operating profit of \$348.1 million for the year ended December 31, 2012, compared to an operating profit of \$279.8 million for the year ended December 31, 2011.

**Interest Income.** For the year ended December 31, 2012 interest income was \$15.9 million, compared to \$11.9 million for the year ended December 31, 2011. The increase was primarily due to an increase in our average cash balance for the year and increases in interest rates.

**Foreign Currency Exchange Loss.** For the year ended December 31, 2012, foreign currency exchange loss was \$0.6 million, compared to \$0.6 million for the year ended December 31, 2011.

**Interest Expense.** For the year ended December 31, 2012, interest expense was \$2.2 million, compared to \$7,000 for the year ended December 31, 2011. The increase was primarily due to interest expense on the bank loans of \$2.1 million.

**Other Income/(Expenses).** For the year ended December 31, 2012, other income/(expense) represent other expense of \$0.2 million, compared to other income of \$0.5 million for the year ended December 31, 2011.

**Income Tax Expense.** Income tax expense was \$67.4 million for the year ended December 31, 2012, compared to \$43.6 million for the year ended December 31, 2011. The increase was in line with the increase in our profit before income tax and withholding tax for distribution of a cash dividend.

**Net Income Attributable to Mezzanine Classified Non-controlling Interest.** In accordance with ASC subtopic 480-10, we calculate, on an accumulative basis from the acquisition date, (i) the amount of accretion that would increase the balance of non-controlling interest to its estimated redemption value over the period from the date of the 7Road acquisition to the earliest redemption date of the non-controlling interest and (ii) the amount of net profit attributable to non-controlling shareholders of 7Road based on their ownership percentage. The carrying value of the non-controlling interest as mezzanine equity will be adjusted by an accumulative amount equal to the higher of (i) and (ii). For the year ended December 31, 2012, the accretion charge was \$11.2 million, compared to \$2.6 million for the year ended December 31, 2011.

**Net Income Attributable to Changyou.com Limited.** As a result of the foregoing, we had net income attributable to Changyou.com Limited of \$282.4 million for the year ended December 31, 2012, compared to net income of \$245.5 million for the year ended December 31, 2011.

#### *Liquidity and Capital Resources*

We have financed our operations primarily through cash flows from equity contributions by Sohu and cash flows from operations. We also received loans in the amount of \$5.0 million and \$3.5 million, respectively, from Sohu.com Limited in September 2007 and December 2008. Such loans were repaid to Sohu in April 2009.

In April 2009, we received net proceeds of \$54.7 million from our initial public offering.

On April 1, 2009, we declared a cash dividend of \$96.8 million payable solely to Sohu.com (Game) Limited, which is an indirect wholly-owned subsidiary of Sohu.com Inc. In the fourth quarter of 2009, after receiving approval from the PRC government, we paid the dividend to Sohu.com (Game) Limited. In connection with such dividend we also paid PRC withholding tax of \$5.0 million.



On August 6, 2012 our Board of Directors declared, and on September 21, 2012 we paid to our shareholders, a special one-time cash dividend in the total amount of \$200.9 million, of which \$136.3 million was paid to Sohu.com (Game) Limited.

During 2012 and 2013, we drew down loans from offshore banks in an aggregate amount of \$410.3 million, which were secured by an equivalent or greater amount of RMB deposits in onshore branches of those banks, totaling \$424.7 million. As of December 31, 2013, \$370.0 million of the loan amount carried a floating rate of interest based on the London Inter-Bank Offered Rate and \$103.3 million carried a fixed rate of interest.

As of December 31, 2013, we had cash and cash equivalents and short-term investments of approximately \$551.3 million. As of December 31, 2012, we had cash and cash equivalents and short-term investments of approximately \$418.4 million. Cash equivalents primarily consist of time deposits with maturities of three months or less.

We believe our current liquidity and capital resources are sufficient to meet anticipated working capital needs (net cash used in operating activities), commitments and capital expenditures over the next twelve months.

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

	For the Year Ended December 31,		
	2011	2012	2013
		(\$ in thousands)	
Net cash provided by operating activities	276,602	340,436	358,643
Net cash used in investing activities	(316,649)	(314,696)	(322,693)
Net cash provided by financing activities	—	8,739	130,102
Effect of exchange rate changes on cash and cash equivalents	19,431	1,749	15,793
Net (decrease) increase in cash and cash equivalents	(20,616)	36,228	181,845
Cash and cash equivalents at beginning of the year	351,027	330,411	366,639
Cash and cash equivalents at end of the year	330,411	366,639	548,484

#### *Operating Activities*

Net cash provided by operating activities for the year ended December 31, 2013 was \$358.6 million, which was primarily attributable to the following factors: (i) net income of \$286.4 million, (ii) depreciation and amortization of \$42.4 million (iii) change in current assets and liabilities of \$21.0 million; and (iv) deferred tax expenses of \$5.4 million.

Net cash provided by operating activities for the year ended December 31, 2012 was \$340.4 million, which was primarily attributable to (i) net income of \$293.6 million, (ii) depreciation and amortization of \$38.0 million, (iii) an increase in deferred tax expense of \$9.7 million.

Net cash provided by operating activities for the year ended December 31, 2011 was \$276.6 million, which was primarily attributable to (i) net income of \$248.0 million, (ii) depreciation and amortization of \$28.8 million, (iii) an increase in receipts in advance and deferred revenue of \$14.9 million.

#### *Investing Activities*

For the year ended December 31, 2013, net cash used in investing activities was \$322.7 million, which was primarily attributable to purchase of fixed assets of \$61.6 million, purchase of intangible assets and other assets of \$34.1 million, cash paid in relation to restricted time deposits of \$168.6 million and cash paid for business acquisitions (net of cash acquired) of \$109.7 million, partially offset by a cash inflow consisting of the proceeds from short-term investments of \$51.2 million.



For the year ended December 31, 2012, net cash used in investing activities was \$314.7 million and was primarily attributable to cash paid in relation to restricted time deposits of \$244.6 million, purchase of short-term investments of \$32.6 million, purchase of intangible assets and other assets for \$22.7 million, and purchase of fixed assets of \$11.7 million.

For the year ended December 31, 2011, net cash used in investing activities was \$316.6 million and was primarily attributable to our payment of the consideration for business acquisitions (net of cash acquired) of \$216.6 million, prepayment of \$62.8 million for an office building, purchase of fixed assets of \$20.6 million, and purchase of intangible assets and other assets for \$16.9 million.

#### *Financing Activities*

For the year ended December 31, 2013, net cash used in financing activities was \$130.1 million, which was primarily due to our receipt of the proceeds of loans from offshore banks of \$167.0 million, payment of contingent consideration of \$19.7 million, payment of \$17.2 million for the repurchases under our share repurchase program.

For the year ended December 31, 2012, net cash provided by financing activities was \$8.7 million, which was primarily due to our receipt of the proceeds of loans from offshore banks of \$239.4 million, a dividend distribution to our shareholders of \$200.9 million, repayment of promissory note of \$16.0 million and payment of contingent consideration of \$13.1 million.

For the year ended December 31, 2011, no net cash was (used in) provided by financing activities.

#### *Restrictions on Cash Transfers to Us*

To fund any cash requirements from time to time, we may need to rely on dividends, loans or advances made by our PRC subsidiaries. We conduct most of our operations in PRC through our VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE, which generate most of our operating revenues. As our VIEs are not owned by our subsidiaries, they are not able to make dividend payments to our subsidiaries. Instead, our subsidiaries AmazGame, 7Road Technology, Gamespace and ICE Information have entered into a number of contracts with their corresponding VIEs to provide services to such VIEs in return for cash payments. In order for us to receive any dividends, loans or advances from AmazGame, 7Road Technology, Gamespace and ICE Information, or to distribute any dividends to our shareholders and ADS holders from operating income sources, we will need to rely on these payments made from our VIEs to AmazGame, 7Road Technology, Gamespace and ICE Information. Depending on the nature of services provided by these PRC subsidiaries to their corresponding VIEs, certain of these payments are subject to PRC taxes, including business taxes and VAT, which effectively reduce the amount that a PRC subsidiary receives from its corresponding VIE. In addition, the PRC government could impose restrictions on such payments or change the tax rates applicable to such payments.

Regulations in the PRC currently permit payment of dividends of a PRC company, such as AmazGame, only out of accumulated profits as determined in accordance with accounting standards and regulations in China. Each of our PRC subsidiaries is also required to set aside at least 10% of its after-tax profit, determined in accordance with PRC accounting standards, each year to its general reserves until the cumulative amount reaches 50% of its registered capital. These reserves are not distributable as cash dividends, or as loans or advances. A PRC company may also allocate a portion of its after-tax profits, as determined by its Board of Directors, to its staff welfare and bonus funds, which may not be distributed to us.

Furthermore, under regulations of the SAFE, the RMB is not convertible into foreign currencies for capital account items, such as loans, repatriation of investments and investments outside of China, unless the prior approval of the SAFE is obtained and prior registration with the SAFE is made.

Any dividends paid by any of our PRC subsidiaries to its direct holding company in Hong Kong will be subject to a withholding tax at a rate of at least 5% and could be as high as 10%, which will reduce the amount of cash available for distribution to us. See “Risk Factors—Risks related to Doing Business in China—There are significant uncertainties under the Corporate Income Tax Law of the PRC, or the CIT Law, regarding our PRC enterprise income tax liabilities, such as tax on dividends paid to us by our PRC subsidiaries. The CIT Law also contains uncertainties regarding possible PRC withholding tax on any dividends we pay to our overseas corporate shareholders and gains realized from the transfer of our shares by our overseas corporate shareholders.” in Item 3.

We do not expect any of such restrictions or taxes to have a material impact on our ability to meet our cash obligations.

We believe that our existing cash is sufficient to sustain our operations for at least the next twelve months.



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**Capital Expenditures**

Our capital expenditures include the purchase of fixed assets, intangible assets and other assets. Our capital expenditures were \$95.7 million, \$34.5 million and \$100.3 million, respectively, for the years ended December 31, 2013, 2012 and 2011.

In August 2010, we entered into agreements with a property developer for the purchase of an office building to be built in Beijing at a price of approximately \$162.4 million. Under the August 2010 agreements, the purchase price was adjusted based on the actual floor area built, the final unit price agreed to by the parties, and cost adjustments, which were agreed to be approximately \$3.2 million, related to changes to the original design of the building. The office building serves as our headquarters and has an area of approximately 56,549 square meters. As of December 31, 2013, we had paid \$165.2 million to the property developer.

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

Our research and development efforts are primarily to keep pace with technological advances in order to make our online game development capabilities and our games competitive in the market. Moreover, we also focus on the improvement of our licensed games. We intend to further expand our internal game development capabilities and license more new games that are attractive to users in China.

**Off-balance Sheet Arrangements**

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

**Contractual Obligations**

The following table sets forth our contractual obligations and commercial commitments as of December 31, 2013 (in thousands):

	<b>Total</b>	<b>Less than 1 Year</b>	<b>1-3 Years</b>	<b>More than 3 Years</b>
Office rental	36,505	9,607	14,482	12,416
Bandwidth leasing charges	8,420	7,578	842	—
Fees for game development services and in-progress games	24,636	6,498	18,138	—
Expenditures for games with technological feasibility	15,214	9,264	5,950	—
Cinema advertisement slot rights	29,695	1,082	18,444	10,169
Others	396	396	—	—
<b>Total</b>	<b>114,866</b>	<b>34,425</b>	<b>57,856</b>	<b>22,585</b>

Other than the obligations set forth above, we did not have any material capital commitments, long-term debt obligations, operating lease obligations, purchase obligations or other long-term liabilities as of December 31, 2013.



## IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In March of 2013, the FASB issued guidance on “Foreign Currency Matters, Parent’s Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity.” The amendments clarify the applicable guidance for the de-recognition of all or a portion of a cumulative translation adjustment when an entity ceases to have a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business (other than a sale of in substance real estate or conveyance of oil and gas mineral rights) within a foreign entity or when other changes stipulated occur and involve a foreign entity. The amendments are effective prospectively for fiscal years (and interim reporting periods within those years) beginning after December 15, 2013. We are currently evaluating the impact on our consolidated financial statements of adopting this guidance.

In March of 2013, the FASB issued guidance on “Income Taxes—Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists.” The amendments clarify that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss, similar tax loss, or tax credit carryforward, except as noted in the following sentence. To the extent a net operating loss, similar tax loss, or tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such a purpose, then under this exception the unrecognized tax benefit is to be presented in the financial statements as a liability and should not be combined with (netted with) the deferred tax asset(s). The assessment of whether a deferred tax asset is “available” is based on the unrecognized tax benefit and deferred tax asset amounts that exist at the reporting date and should be made presuming disallowance of the tax position at the reporting date. The amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. We are currently evaluating the impact on our consolidated financial statements of adopting this guidance.

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### *Directors and Senior Management*

The following table sets forth information regarding our directors and executive officers as of the date of this annual report. The business address of each of our directors and executive officers is East Tower, Jing Yan Building, No. 29 Shijingshan Road, Shijingshan District, Beijing 100043, People’s Republic of China.

Directors and Executive Officers	Age	Position
Charles Zhang	49	Chairman of the Board of Directors
Tao Wang	38	CEO and Director
Dewen Chen	38	President
Alex Ho (1)	39	Chief Financial Officer
Xiaojian Hong	36	Chief Operating Officer
Wendy Pan	46	Chief Information Officer
Dave De Yang (2)	48	Independent Director
Xiao Chen (2)	50	Independent Director
Charles Chan (2)	60	Independent Director

- (1) Mr. Alex Ho has resigned as our Chief Financial Officer, effective March 4, 2014. Ms. Erin Sheng, currently our finance director, will assume the role of interim chief financial officer following Mr. Ho’s departure. We are in the process of searching for a permanent chief financial officer.
- (2) Member of the audit committee of our Board of Directors.

*Dr. Charles Zhang* is the Chairman of our Board of Directors. Dr. Zhang is the founder of Sohu and has been Chairman of the Board and CEO of Sohu since August 1996. Prior to founding Sohu, Dr. Zhang worked for Internet Securities Inc., or ISI, and helped establish its China operations. Prior to joining ISI, he worked as Massachusetts Institute of Technology’s liaison officer with China. Dr. Zhang has a Ph.D. in Experimental Physics from the Massachusetts Institute of Technology and a bachelor of science degree from Tsinghua University in Beijing.





*Tao Wang* is our CEO and a director. Mr. Wang has over 16 years of experience in the computer game industry in China and was one of the principal founders of our online game business. Prior to our carve-out from Sohu, Mr. Wang served as Sohu's Vice President of MMORPG business. Mr. Wang joined Sohu in December 2004 and was instrumental in the ramp up of our MMORPG business and played a key role in the success of TLBB. Prior to joining Sohu, Mr. Wang worked at Sina and was the Managing Technology Director for its iGAME development and operations. From 2001 to 2003, Mr. Wang served as the Vice President and Chief Technology Officer of Beijing Tian Ren Interactive Software Technologies Co. Ltd., a PRC games distributor and operator. From 1998 to 2001, Mr. Wang was a project manager at Object Software (Beijing) Limited, one of the pioneer games and multi-media software developers in China, responsible for its PC console games, Internet games and multi-media educational software development. From 1997 to 1998, Mr. Wang worked at Fuzhou Wai Xin Software Technologies Co. Ltd. as a software development engineer. Mr. Wang received a bachelor's degree in Engineering from Hangzhou Industrial Electronics Institute.

*Dewen Chen* is our President and was one of the principal founders of our online game business. Mr. Chen joined Sohu in 2005 as a business manager, responsible for building our sales team for games products and starting May 2006, Mr. Chen was in charge of the overall marketing, promotion, sales and channel distribution of Sohu's games products. Prior to our carve out from Sohu, Mr. Chen was the Director of Marketing & Operations of the MMORPG business of Sohu. From April 2000 to April 2005, Mr. Chen worked at Shanghai Hua Teng Software System Co. Ltd. as a pre-sale technology consultant and sale manager of its business with banks. Prior to that, Mr. Chen had worked with Fujian Shi Da Computer Group as a software engineer, project manager and later the Director of the Technology Department at its Shanghai branch office. Mr. Chen received a bachelor's degree in Computer Engineering from Xi'an Jiaotong University.

*Alex Ho* is our Chief Financial Officer. Prior to our initial public offering, Mr. Ho was the Senior Finance Director of Sohu, which he joined in January 2005. Prior to joining Sohu, Mr. Ho worked at Arthur Andersen & Co. and PricewaterhouseCoopers in Hong Kong and Beijing, where he was a Senior Manager of Assurance and Business Advisory. With an extensive knowledge of and background in both U.S. and Chinese accounting principles and tax laws, financial management and SEC reporting, Mr. Ho has helped companies through executing mergers and acquisitions in Asia, restructuring businesses, completing the initial public offering process for international markets, as well as compliance with Section 404 of the Sarbanes-Oxley Act of 2002. Mr. Ho received a bachelor's degree in Finance and Accounting from the University of Hong Kong and an EMBA degree from Tsinghua University. Mr. Ho is a member of the American Institute of Certified Public Accountants and the Hong Kong Institute of Certified Public Accountants.

*Xiaoian Hong* is our Chief Operating Officer and was one of the principal founders of our MMORPG business. Mr. Hong has significant experience in the security, efficiency and stability of online games software and operations. Prior to our carve-out from Sohu, Mr. Hong was a Senior Manager of Sohu and played a key role in building Sohu's MMORPG software development division and was responsible for strategic planning for technology framework design and module development for our MMORPG business. From 2004 to 2005, Mr. Hong worked at Sina and was a research and development manager of its iGAME project. From 2001 to 2004, Mr. Hong was the Manager of Research and Development of Beijing Tian Ren Interactive Software Technologies Co. Ltd., responsible for in-house digital games design and development and introduction, distribution and localization of popular overseas games products. From 1999 to 2001, Mr. Hong was a project manager of Object Software (Beijing) Limited. Mr. Hong received a bachelor's degree in Engineering from Beijing Technology University.

*Wendy Pan* is our Chief Information Officer. Ms. Pan joined us in January 2013 and is primarily responsible for leading the development of our operational performance management system and managing the implementation of our business strategies. Prior to joining us, from 1997 to 2012, Ms. Pan worked as a senior executive at Huawei Technology Co., Ltd., where she was mainly responsible for managing the execution of Huawei's strategies in certain areas and for project management, as well as leading teams on transformational projects that included the implementation of IPD (integrated product development) and IFS (integrated financial services). She has experience in strategic decoding and planning and played a leading role in designing and implementing construction management systems. Prior to joining Huawei Technology Co., Ltd., Ms. Pan worked as a development engineer and a factory branch director in the Sichuan Posts and Telecommunications Equipment Factory from 1989 to 1997. Ms. Pan received her bachelor's degree in automatic control from Haerbin College of Shipbuilding Engineering in 1989.

*Dave De Yang* has served as an independent director and a member of our audit committee since April 2009. Mr. Yang has been serving a role of CFO for Reckitt Benckiser North Asia region including China, Hong Kong, Taiwan, Japan and Korea since September 2012. Prior to this role, Mr. Yang had worked for McDonald's Corporation as a senior financial director, including an international assignment as the Corporate Controller of McDonald's China for three and half years. Prior to such role, he served as acting controller of McDonald's India and Indonesia and as a senior director of McDonald's Corporation in Asia Pacific, Middle East and Africa division where he oversaw the development and supervision of financial strategy and policy. Prior to joining McDonald's Corporation, Mr. Yang worked in the U.S. business unit of Ernst & Young LLP for seven years in various positions, including as a group manager. During Mr. Yang's tenure at Ernst & Young LLP, he focused on business risk management consultation, corporate M&A, restructuring of corporate internal management processes, internal audits, risk assessment, control system designs, and auditing of corporate financial statements, primarily for Fortune 500 companies. Mr. Yang has a master of business administration degree from the City University of New York, a master's degree in Management and Engineering from the Graduate School of the Chinese Academy of Sciences in Beijing, and a bachelor's degree in Physics from the University of Science and Technology of China. Mr. Yang is a member of the U.S. Institute of Certified Internal Auditors, the Institute of Certified Public Accountants and the Institute of Certified Management Accountants.



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*Dr. Xiao Chen* has served as an independent director and a member of our audit committee since August 2012. Dr. Chen is a professor in the Department of Accounting of the School of Economics and Management at Tsinghua University. For the past 15 years, he has been teaching and conducting academic research in the fields of accounting and taxation at Tsinghua University. He is a board member of the China Accounting Society and the China International Taxation Society. Since August 2007, Dr. Chen has served on the board of directors and as the chairman of the audit committee of Noah Education Holdings Ltd, a public company listed on the New York Stock Exchange. Since 2011, he has also served as an independent director of China First Chemical Holdings Ltd, a company listed on Hong Kong Stock Exchange. Prior to 2012, he served as an independent director of five public companies listed on the Shanghai and Shenzhen Stock Exchanges. Dr. Chen received a bachelor's degree in engineering from the Wuhan Institute of Chemical Engineering in 1983, a master's degree in management from the University of Science and Technology of China in 1989, and a Ph.D. in economics from Tulane University in 1996.

*Mr. Charles Chan* has served as an independent director and a member of our audit committee since September 2013. Mr. Chan joined Arthur Andersen Canada in 1977 and was admitted to the AA Worldwide Partnership in 1988. Transferred to Arthur Andersen Hong Kong/China in 1994, Mr. Chan was Head of Audit and Business Advisory Service for Greater China. After Arthur Andersen merged with PricewaterhouseCoopers, or PwC, in 2002, Mr. Chan assumed management positions at PwC, including as a partner and as a member of various committees. Mr. Chan qualified as a Chartered Accountant in Canada in 1980 and as a Certified Public Accountant in Hong Kong in 1995. He has extensive experience in serving major clients listed in various major capital markets through the IPO process, conducting annual audits, providing business advice with respect to M&A activities and various types of capital and debt financing transactions. Mr. Chan has served as a member of professional, government and regulatory committees, including the Hong Kong Stock Exchange Listing Committee, the Selection Committee for the first Legislative Council of the Hong Kong SAR and the Hong Kong Society of Certified Public Accountants. For the Hong Kong Society of Certified Public Accountants, he served as a member of its council, accounting standards committee and auditing standards committee, and was chairman of its China technical committee. Mr. Chan retired from PwC on June 30, 2012.

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

For the year ended December 31, 2013, we paid an aggregate of approximately \$9.1 million in cash compensation to our executive officers. We paid an aggregate of \$0.2 million in cash compensation to our non-executive directors other than Dr. Charles Zhang. None of our directors have service contracts that provide for benefits upon termination of employment. For information regarding share-based compensation paid to officers and directors, see Item 6, "Directors, Senior Management and Employees—Compensation of Directors and Executive Officers—Share Incentive Plan."

#### ***Employment Agreements with Executive Officers***

We have entered into employment agreements with each of our executive officers. Under these agreements, we may terminate an executive officer's employment for cause, at any time, for certain acts of such officer such as willful misconduct or gross negligence, repeated failure to perform substantially his duties, indictment or conviction for or confession of a felony, or any crime involving moral turpitude. In such case, such officer will not be entitled to receive payment of any severance benefits or other amounts by reason of termination other than accrued salary and vacation through the date of termination and such officer's right to all other benefits will terminate, except as required by any applicable law.

We may also terminate our employment agreements with our executive officers without cause upon thirty-day advance written notice. In such case of termination by us and also in a case where an executive officer voluntarily terminates his employment with us upon thirty-days' advance written notice for "good reasons," we are required to provide him with severance benefits equal to an amount up to six (6) months of his monthly base salary, provided that such executive officer complies with the "employee non-competition, non-solicitation, confidential information and work product agreement" during the severance period and execute a release agreement in the form requested by us. "Good reasons" include (i) any significant change in the executive officer's duties and responsibilities inconsistent in any material and adverse respect with his title and position, and (ii) any material breach of the employment agreement by us, including any reduction in the executive officer's base salary or our failure to pay to him any portion of his compensation.

In addition, each of our executive officers has entered into an employee non-competition, non-solicitation, confidential information, and work product agreements with us. Under these agreements, each of our executive officers has agreed to be bound by (i) non-competition restrictions during his employment and for one year after the termination of his employment or for such longer period during which we pay him any severance benefits, and (ii) non-solicitation restrictions during the non-competition period. Each executive officer has agreed to hold, both during and after the termination or expiry of his employment agreement, in strict confidence and not to use, except as required in the performance of his or her duties in connection with the employment, any of our confidential information or trade secrets, any confidential information or trade secrets of our clients or customers, or the confidential or proprietary information of any third party held by us in confidence. The executive officers have also agreed to disclose to us all inventions which they conceive and develop during the employment and to assign all right, title and interest in them to us and agreed not to assert any such rights against us.



## *Share Incentive Plan*

### *Changyou.com Limited 2008 Share Incentive Plan*

In December 2008, our Board of Directors and our shareholders adopted our 2008 Share Incentive Plan to attract, motivate and retain the best available personnel, provide additional incentives to our employees, directors and consultants and promote the success of our business. Our 2008 Share Incentive Plan provides for the issuance of up to 20,000,000 ordinary shares, of which 17,740,000 are Class B ordinary shares and 2,260,000 are Class A ordinary shares.

*Plan Administration.* Our Board of Directors or our compensation committee administers our share incentive plan and determines the terms and conditions of awards.

*Types of Awards.* The following is a summary of the awards that may be granted under our 2008 Share Incentive Plan.

- *Options.* Provide for the right to purchase our ordinary shares at a specified exercise price subject to vesting, and generally will become exercisable in four equal annual installments beginning on the first anniversary of the date of grant.
- *Restricted Shares.* A sale of ordinary shares at a price determined by our board or our compensation committee or a grant of our ordinary shares, in each case subject to vesting terms.
- *Restricted Share Units.* Represent the right to receive our ordinary shares, subject to vesting. Restricted share units will generally be settled upon vesting, either by our delivery to the holder of the number of ordinary shares that equals the number of the vested restricted share units or by a cash payment to the holder that equals the then fair market value of the number of underlying ordinary shares. If any of the restricted share units that are settleable in Class B ordinary shares expire without settlement, such underlying Class B ordinary shares will be automatically converted into Class A ordinary shares and such Class A ordinary shares so converted will become available for future issuance under our 2008 Share Incentive Plan.

*Award Document.* Awards granted under our share incentive plan are evidenced by an award document that sets forth the terms and conditions applicable to each of these awards, as determined by our board or compensation committee in its sole discretion.

*Termination of the Share Incentive Plan.* Our share incentive plan will terminate in August 2018. Our Board of Directors may amend, suspend, or terminate our 2008 Share Incentive Plan at any time; provided, however, that our Board of Directors must first seek the approval of the participants of our share incentive plan if such amendment, suspension or termination would adversely affect the rights of participants with respect to any of their existing awards.

### *Conversion Cash Bonus Plan*

On July 10, 2012, 7Road adopted the 7Road 2012 Share Incentive Plan, which initially provided for the issuance of up to 5,100,000 Class A ordinary shares of 7Road (amounting to 5.1% of the then outstanding 7Road shares on a fully-diluted basis) to selected directors, officers, employees, consultants and advisors of 7Road. On November 2, 2012, the number of Class A ordinary shares available for issuance under the 7Road 2012 Share Incentive Plan was increased to 15,100,000 shares

In July 2012, 7Road granted restricted share units settleable upon vesting by the issuance of an aggregate of 2,546,250 Class A ordinary shares of 7Road, with vesting in installments of 40%, 30% and 30%, respectively, on the first, second and third anniversaries of the grant date and vesting subject to the additional conditions that 7Road complete a firm commitment underwritten initial public offering of its Class A ordinary shares resulting in a listing on an internationally recognized exchange and all underwriters' lockup periods applicable to such offering expire.

On June 28, 2013, 7Road's Board of Directors approved the cancellation of the 7Road 2012 Share Incentive Plan. 7Road concurrently offered to a total of 42 7Road employees holding an aggregate of 2,223,750 restricted share units which had been granted under the 7Road 2012 Share Incentive Plan the right to exchange their restricted share units for, at each employee's election, in each case subject to the employee's continued employment by 7Road, either (i) the right to a cash payment of up to an aggregate of \$2.90 per restricted share unit exchanged, vesting and payable at the rate of 40%, 30% and 30%, respectively, on the first, second and third anniversaries of July 18, 2012, which is the date when the surrendered restricted share units were granted under the 7Road 2012 Share Incentive Plan, or (ii) the right to receive an annual cash bonus, over a seven-year period commencing July 1, 2013, based on adjusted annual cumulative net income of 7Road. All restricted share units held by these 42 holders under the 7Road 2012 Share Incentive Plan as of June 28, 2013 were included in this exchange program.

### *Employee Incentive Plans*

On February 8, 2014, our Board of Directors approved three new employee incentive plans with terms of 10 years, under which we may pay compensation to employees based on our profits, or the profits of specified projects.

Eligible employees will receive a cash award from the plans as a bonus based on the number of employee incentive instruments they hold in the plans. Under each of two of the plans, we will distribute to eligible employees who participate in the plans up to 5% of our annual adjusted net profits. Combined, these two plans will distribute up to 10% of our annual adjusted net profits. The third employee incentive plan is structured to allow eligible employees on a specified project to receive up to 20% of the adjusted net profits of the specified project.

Eligible employees will participate in these plans by paying an amount to purchase instruments that will entitle them, while they are employed by us, to receive annual compensation under the plan. After fulfilling certain conditions, employees will be entitled to sell their instruments to other employees at any time during their employment with us at a negotiated price or sell their instruments back to us, subject to certain conditions, at the principal amount when they leave the company.

The Company's management believes the implementation of these plans will grant these employees a sense of ownership in the Company and encourage an entrepreneurial spirit, as well as provide additional incentive to participating employees to work toward strong results within their areas of responsibility.

### *Issuance of Restricted Shares and Restricted Share Units to Executive Officers*

On January 15, 2009, 8,000,000 Class B restricted shares were issued out of Sohu.com (Game) Limited's equity interest in us to Prominence Investments Ltd., or Prominence, a British Virgin Islands company beneficially owned by Tao Wang, our CEO. The restricted shares were subject to vesting over a four-year period commencing on February 1, 2008, and were subject to forfeiture to Sohu.com (Game) Limited if the vesting conditions were not met. All of such Class B restricted shares had been vested as of the date of this annual report. During the period from February 1, 2012 through January 31, 2015, however, Prominence may not, directly or indirectly, transfer, assign, pledge or otherwise dispose of the 2,000,000 Class B restricted shares that became vested on February 1 2012, and if during that period Mr. Wang breaches any of the non-competition, non-solicitation or non-infringement covenants contained in the share subscription agreement under which the Class B restricted shares were issued, such 2,000,000 shares will be forfeited to Sohu.com (Game) Limited. Also see "Operating And Financial Review And Prospects—Operating Expenses—Share-based Compensation Expenses" in Item 5.

On January 15, 2009, we issued to our executive officers other than Tao Wang an aggregate of 1,800,000 of our Class B restricted shares. On March 13, 2009, we exchanged these Class B restricted shares for restricted share units (setttable in Class B ordinary shares). The vesting of these restricted share units was contingent upon the completion of an initial public offering by us on an internationally recognized stock exchange, and the restricted share units are otherwise subject to vesting over a four-year period, subject to acceleration under certain circumstances, commencing February 1, 2008. On April 21, 2009, we granted to our executive officers other than Tao Wang an aggregate of 1,200,000 of our Class A restricted share units. These restricted share units are subject to vesting over a four-year period and will be forfeited to us if the vesting conditions are not met. See "Operating And Financial Review And Prospects—Operating Expenses—Share-based Compensation Expenses."

As of December 31, 2013, we had granted the following restricted shares and restricted share units to our directors and executive officers pursuant to our 2008 Share Incentive Plan.

<u>Directors and Executive Officers</u>	<u>Restricted Shares and Restricted Share Units</u>	<u>Date of Grant</u>	<u>End of Vesting Period</u>
Tao Wang	8,000,000 <sup>(1)</sup>	January 15, 2009	February 1, 2012
Dewen Chen	750,000 <sup>(2)</sup>	January 15, 2009	February 1, 2012
	500,000 <sup>(3)</sup>	April 21, 2009	April 21, 2013
Alex Ho	* <sup>(2)</sup>	January 15, 2009	February 1, 2012
	* <sup>(3)</sup>	April 21, 2009	April 21, 2013
Xiaojian Hong	750,000 <sup>(2)</sup>	January 15, 2009	February 1, 2012
	500,000 <sup>(3)</sup>	April 21, 2009	April 21, 2013
Wendy Pan	* <sup>(3)</sup>	January 7, 2013	January 7, 2013

(1) Class B restricted shares. As of December 31, 2013, 8,000,000 of such Class B restricted shares have become vested and are no longer subject to forfeiture.

(2) Restricted share units settleable in Class B ordinary shares, which have vested and are no longer subject to forfeiture.

(3) Restricted share units settleable in Class A ordinary shares, which have vested and are no longer subject to forfeiture.

\* Less than 1% of our total outstanding voting securities.





### ***Board of Directors***

Our Board of Directors currently consists of Dr. Charles Zhang, Tao Wang, Dave De Yang, Xiao Chen and Charles Chan. Our directors are elected by the holders of our ordinary shares and will hold office until our next annual general meeting of shareholders and until their successors are duly elected or appointed, or until their resignation or removal in accordance with the provisions of our memorandum and articles of association. Baoquan Zhang, who had been a member of our board of directors since April 2009, did not stand for re-election at our annual general meeting of shareholders held in September 2013 and Charles Chan was elected as a director by our shareholders at the meeting. A director is not required to hold any shares in our company by way of qualification. A director may vote with respect to any contract, proposed contract or arrangement in which he is materially interested provided that the nature of such interest is disclosed prior to any vote thereon. A director may exercise all the powers of our company to borrow money, mortgage or charge our undertakings, property and uncalled capital or any part thereof, and issue debentures or other securities whether outright or as security for any debt, liability or obligation of our company or of any third party.

A company of which more than 50% of the voting power is held by a single entity is considered a “controlled company” under the NASDAQ Listing Rules. A controlled company need not comply with the applicable NASDAQ corporate governance rules requiring its Board of Directors to have a majority of independent directors and independent compensation and corporate governance and nominating committees. Because more than 50% of the voting power of our company is held by Sohu, we qualify as a “controlled company” under the NASDAQ Listing Rules, and we avail ourselves of the controlled company exception provided under those rules. In the event that we are no longer a controlled company, a majority of our Board of Directors will be required to be independent and it will be necessary for us to have compensation and corporate governance and nominating committees that are composed entirely of independent directors, subject to a phase-in period during the first year we cease to be a controlled company, unless we invoke the home country exception to such requirement available to foreign private issuers, such as us, under the NASDAQ Listing Rules.

### ***Committees of the Board of Directors***

**Audit Committee.** Our audit committee currently consists of Dave De Yang, Xiao Chen and Charles Chan. Dr Baoquan Zhang, who had been a member of our audit committee since April 2009, ceased to be a director and a member of our audit committee in September 2013 after his term expired and Mr. Chan, after his election as a director, was appointed by our board of directors to be a member of our audit committee to fill the vacancy created by Mr. Zhang’s departure. Our Board of Directors has determined that Dave De Yang, Xiao Chen and Charles Chan satisfy the independence requirements of Rule 10A-3 under the Securities Exchange Act of 1934 and Rule 5605 of the NASDAQ Listing Rules. In addition, our Board of Directors has determined that Dave De Yang meets the criteria of an audit committee financial expert as set forth under the applicable SEC rules and Rule 5605(c)(2) of the NASDAQ Listing Rules. The full responsibilities of our audit committee are set forth in its charter, which will be reviewed and updated annually and approved by our board, and will be posted on our Website at [www.changyou.com](http://www.changyou.com). The audit committee is responsible for, among other things:

- selecting the independent auditors and pre-approving all auditing and non-auditing services permitted to be performed by the independent auditors;
- overseeing our accounting and financial reporting processes and audits of the financial statements of our company;
- reviewing with the independent auditors any audit problems or difficulties and management’s response;
- reviewing and approving all proposed related party transactions, as defined in Item 404 of Regulation S-K under the Securities Act and in the NASDAQ Listing Rules;
- discussing the annual audited financial statements with management and the independent auditors;
- reviewing major issues as to the adequacy of our internal controls over financial reporting and any special audit steps adopted in the light of any significant deficiencies or materially weakness in our internal controls; and
- meeting separately and periodically with management and the independent auditors.

### ***Duties of Directors***

Under Cayman Islands law, our directors have a common law duty to act honestly in good faith with a view to our best interests and for a proper purpose. Our directors also have a duty to exercise the skill they actually possess with the care and diligence that a reasonably prudent person would exercise in comparable circumstances. In fulfilling their duty of care to us, our directors must ensure compliance with our memorandum and articles of association. A shareholder in our name may have the right to seek various remedies in our name if a duty owed by our directors is breached.

### ***Terms of Directors and Officers***

A director may be removed by ordinary resolution passed by a majority of our shareholders before the expiration of such director’s term. Officers are elected by and serve at the discretion of the Board of Directors.





### Employees

As of December 31, 2011, 2012, and 2013, we had 3,297, 4,414 and 6,106 full-time employees, respectively. The following table sets forth the number of our employees by department as of December 31, 2013:

	As of December 31, 2013	
	Number	Percentage
Product development	3,139	51.4%
Game operations <sup>(1)</sup>	953	15.6%
Sales and marketing	857	14.0%
Customer service	237	3.9%
General and administration	920	15.1%
Total	6,106	100%

(1) Includes technical support employees.

In addition, as of December 31, 2013, we had 109 part-time employees. None of our employees are represented by a labor union. None of our employees are represented under collective bargaining agreements.

### Share Ownership

Refer to “Item 7: Major Shareholders and Related Party Transactions” below for a description of the share ownership of our directors and senior executive officers.

## ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

### Major Shareholders

The following table sets forth information with respect to the beneficial ownership of our shares as of February 21, 2014 by:

- each of our directors and executive officers; and
- each person known to us to own beneficially more than 5% of our shares.

	Ordinary Shares Beneficially Owned <sup>(1)</sup>	
	Number	%
<b>Directors and Executive Officers:</b>		
Charles Zhang	*	*
Tao Wang <sup>(2)</sup>	14,040,000	13.3%
Dewen Chen	*	*
Alex Ho	*	*
Xiaojian Hong	*	*
Wendy Pan	*	*
Dave De Yang	—	—
Xiao Chen	—	—
Charles Chan	—	—
<b>Principal Shareholder:</b>		
Sohu.com (Game) Ltd. <sup>(3)</sup>	71,750,000	67.9%
Prominence Investments Ltd. <sup>(2)</sup>	14,040,000	13.3%

\* Less than 1% of our total outstanding voting securities.

(1) Includes the number of Class A ordinary shares and percentage ownership represented by Class A ordinary shares determined to be beneficially owned by a person or entity in accordance with rules of the SEC. Holders of Class B ordinary shares may convert their Class B ordinary shares into the same number of Class A ordinary shares at any time and, accordingly, are deemed to beneficially own such Class A ordinary shares. The number of Class A ordinary shares or Class B ordinary shares beneficially owned by a person or entity includes restricted share units that will vest within 60 days after February 28, 2014. Class A ordinary shares or Class B ordinary shares issuable upon the vesting of restricted share units are deemed outstanding for the purpose of computing the percentage of outstanding Class A ordinary shares owned by that person or entity. Such Class A ordinary shares or Class B ordinary shares issuable upon such vesting are not deemed outstanding, however, for the purpose of computing the percentage ownership of any other person or entity.



- (2) Consists of 12,240,000 Class B ordinary shares and 1,800,000 Class A ordinary shares held of record by Prominence. Prominence is a British Virgin Islands company which is ultimately owned by a trust of which Tao Wang, our CEO, is the primary beneficiary. The business address of Prominence Investments Ltd. is c/o Credit Suisse Trust, Singapore, 1 Raffles Link #05-02, Singapore. All of the shares beneficially held by Mr. Wang were vested as of the date of this annual report. The 12,240,000 Class B ordinary shares and 1,800,000 Class A ordinary shares held of record by Prominence represent approximately 14.6% of the voting power of all issued and outstanding ordinary shares of Changyou.
- (3) Consists of 1,500,000 Class A ordinary shares, which are represented by 750,000 ADSs, and 70,250,000 Class B ordinary shares held by Sohu.com (Game) Limited. Sohu.com (Game) Limited, a Cayman Islands corporation and an indirect wholly-owned subsidiary of Sohu.com Inc. The registered address of Sohu.com (Game) Limited is Floor 4, Willow House, Cricket Square, P O Box 2804, Grand Cayman KY1-1112, Cayman Islands. The Class A ordinary shares (represented by ADSs) and the Class B ordinary shares held by Sohu.com (Game) Ltd. collectively represent approximately 83.0% of the voting power of all issued and outstanding ordinary shares of Changyou.

Our ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. With respect to matters requiring a shareholder vote, holders of Class A ordinary shares and holders of Class B ordinary shares vote together as one class. Each Class A ordinary share is entitled to one vote and each Class B ordinary share is entitled to ten votes. We issued Class A ordinary shares represented by our ADSs in our initial public offering. Holders of Class B ordinary shares may choose to convert their Class B ordinary shares into the same number of Class A ordinary shares at any time. Class B ordinary shares are only transferable to an affiliate of the holder or to an affiliate of us.

All of 23,202,686 Class A ordinary shares issued and outstanding as of February 21, 2014, or approximately 22.0% of the combined total of our outstanding Class A and Class B ordinary shares, were held by a single holder of record in the United States, the Bank of New York Mellon, the depository for our ADS program.

#### ***Related Party Transactions***

As of February 21, 2014, Sohu held approximately 67.9% of the combined total of Changyou's outstanding Class A and Class B ordinary shares and controlled approximately 83.0% of the total voting power in Changyou. As of December 31, 2013, Sohu continues to have the power acting alone to approve any action requiring a vote of the majority of our ordinary shares and to elect all our directors.

#### ***Contractual Arrangements with our VIEs and their Shareholders***

PRC law currently restricts foreign ownership of online game businesses. To comply with PRC law, we conduct a significant part of our game operations and distribution businesses and the 17173 Business through contractual arrangements between our PRC subsidiaries AmazGame, 7Road Technology, Gamespace and ICE Information and their corresponding VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE and their respective shareholders. The equity interests in each of Gamease and Guanyou Gamespace are owned 60% by Tao Wang, our Chief Executive Officer, and 40% by Dewen Chen, our President. The equity interests in Shenzhen 7Road are owned 100% by our VIE Gamease, which is a PRC company. The equity interests in Shanghai ICE are owned by Runa Pi and Rong Qi, each of whom holds 50% of Shanghai ICE. The following is a summary of the agreements currently in effect:

#### ***Contractual Arrangements with Gamease and its Shareholders***

- ***Loan Agreements***, between AmazGame and Gamease shareholders. These loan agreements provide for loans of \$906,000 to Tao Wang and of \$604,000 to Dewen Chen for them to make contributions to the registered capital of Gamease in exchange for the 60% and 40% equity interests, respectively, in Gamease. The loans are interest free and are repayable on demand, but the shareholders can only repay the loans by transferring to AmazGame of their respective equity interests in Gamease.
- ***Equity Interest Purchase Right Agreements***, among AmazGame, Gamease and Gamease shareholders. Pursuant to these agreements, AmazGame and any third party designated by AmazGame have the right, exercisable at any time during the term of the agreement, if and when it is legal to do so under PRC law, to purchase from Tao Wang or Dewen Chen, as the case may be, all or any part of his or her equity interests in Gamease at a purchase price equal to their initial contributions to the registered capital of Gamease or the respective proportion of such initial contribution in the case of a partial purchase of such equity interests in Gamease.



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- *Equity Pledge Agreements*, among AmazGame, Gamease and the shareholders of Gamease. Pursuant to these agreements, Tao Wang and Dewen Chen pledged to AmazGame their equity interests in Gamease to secure the performance of their respective obligations and Gamease's obligations under the various VIE-related agreements. If any of the shareholders of Gamease breaches his or her respective obligations under any VIE-related agreements (Gamease's breach of any of its obligations under the various VIE-related agreements will be treated as the shareholders' breach of their respective obligations), including the Equity Pledge Agreement, AmazGame is entitled to exercise its rights as the beneficiary under the Equity Pledge Agreement, including all the rights such shareholder has as a shareholder of Gamease.
- *Business Operation Agreement*, among AmazGame, Gamease and the shareholders of Gamease. This agreement sets forth the rights of AmazGame to control the actions of the shareholders of Gamease.
- *Powers of Attorney*, executed by the shareholders of Gamease in favor of AmazGame. These powers of attorney give AmazGame the exclusive right to appoint nominees to act on behalf of each of the two Gamease shareholders in connection with all actions to be taken by Gamease.
- *Technology Support and Utilization Agreement*, between AmazGame and Gamease. Pursuant to this agreement, AmazGame has the exclusive right to provide certain product development and application services and technology support to Gamease for a fee equal to a predetermined percentage of Gamease's revenues.
- *Services and Maintenance Agreement*, between AmazGame and Gamease. Pursuant to this agreement, AmazGame provides marketing, staffing, business operation and maintenance services to Gamease in exchange for a fee equal to the cost of providing such services plus a predetermined margin.

#### *Contractual Arrangements with Shenzhen 7Road and its Sole Shareholder Gamease*

- *Amended and restated equity interest purchase right agreement* among 7Road Technology, Shenzhen 7Road and Gamease, which is Shenzhen 7Road's sole shareholder. Under this agreement, 7Road Technology and any third-party designated by 7Road Technology have the right, exercisable at any time during the term of the agreement, if and when it is legal to do so under PRC law, to purchase from Gamease all or any part of its shares in Shenzhen 7Road at a nominal purchase price. This agreement has a term of 10 years, is renewable by 7Road Technology for such term as it may determine and is terminable by 7Road Technology by notice to the other parties at any time when, under PRC law as then in effect, 7Road Technology cannot exercise its purchase right, and is also terminable if Shenzhen 7Road's or 7Road's existence is terminated, by mutual agreement of the parties or upon the written request of 7Road Technology. Neither Gamease nor Shenzhen 7Road has any power to terminate the agreement.
- *Amended and Restated Equity Interest Pledge Agreement* among 7Road Technology, Shenzhen 7Road and Gamease. Under this agreement, Gamease agreed to pledge to 7Road Technology Gamease's equity interests in Shenzhen 7Road to secure the performance of Gamease's obligations and Shenzhen 7Road's obligations under the various VIE-related agreements. If Gamease or Shenzhen 7Road breaches its obligations under any VIE-related agreements, 7Road Technology is entitled to exercise its rights as the beneficiary under the Equity Interest Pledge Agreements. This agreement terminates only after all of the obligations of Gamease and/or of Shenzhen 7Road under the various VIE-related agreements are no longer in effect.
- *Amended and Restated Business Operation Agreement* among 7Road Technology, Shenzhen 7Road and Gamease. This agreement grants to 7Road Technology the right to control the actions of Shenzhen 7Road and to control the actions of Gamease in its capacity as the sole shareholder of Shenzhen 7Road. This agreement has an initial term of 10 years, is renewable by 7Road Technology for such term as it may determine and is terminable early if the existence of Shenzhen 7Road or 7Road Technology is terminated, or upon 30 days' advance written notice of 7Road Technology to Shenzhen 7Road.
- *Power of Attorney* executed by Gamease in favor of 7Road Technology. This power of attorney gives 7Road Technology the exclusive right to appoint designees to act on behalf of Gamease in connection with all actions to be taken by Shenzhen 7Road requiring shareholder approval.
- *Technology Development and Utilization Service Agreement* between 7Road Technology and Shenzhen 7Road. Under this agreement, 7Road Technology has the exclusive right to provide product development and application services and technology support to Shenzhen 7Road for a fee based on Shenzhen 7Road's revenues, that is not less than a majority of Shenzhen 7Road revenues for the contract period. The fee can be adjusted by 7Road Technology at any time in its sole discretion. This agreement will terminate if the existence of 7Road Technology or Shenzhen 7Road is terminated, by mutual agreement of the parties or upon failure to perform due to a force majeure event.
- *Services and Maintenance Agreement* between 7Road Technology and Shenzhen 7Road. Pursuant to this agreement, 7Road Technology provides marketing and maintenance services to Shenzhen 7Road in exchange for a fee equal to the cost of providing such services plus a predetermined margin. This agreement will terminate if the existence of 7Road Technology or Shenzhen 7Road is terminated, by mutual agreement of the parties or upon failure to perform due to a force majeure event.



*Contractual Arrangements with Guanyou Gamespace and its Shareholders*

- *Loan Agreements*, between Gamespace and Guanyou Gamespace shareholders. These loan agreements provide for loans of \$906,000 to Tao Wang and of \$604,000 to the Dewen Chen for them to make contributions to the registered capital of Guanyou Gamespace in exchange for the 60% and 40% equity interests, respectively, in Guanyou Gamespace. The loans are interest free and are repayable on demand, but the shareholders can only repay the loans by transferring to Gamespace of their respective equity interests in Guanyou Gamespace.
- *Equity Interest Purchase Right Agreements*, among Gamespace, Guanyou Gamespace and Guanyou Gamespace's shareholders. Pursuant to these agreements, Gamespace and any third party designated by Guanyou have the right, exercisable at any time during the term of the agreement, if and when it is legal to do so under PRC law, to purchase from Tao Wang or Dewen Chen, as the case may be, all or any part of his or her equity interests in Guanyou Gamespace at a purchase price equal to their initial contributions to the registered capital of Guanyou Gamespace or the respective proportion of such initial contribution in the case of a partial purchase of such equity interests in Guanyou Gamespace.
- *Equity Pledge Agreements*, among Gamespace, Guanyou Gamespace and the shareholders of Guanyou Gamespace. Pursuant to these agreements, Tao Wang and Dewen Chen pledged to Gamespace their equity interests in Guanyou Gamespace to secure the performance of their respective obligations and Guanyou Gamespace's obligations under the various VIE-related agreements. If any of the shareholders of Guanyou Gamespace breaches his or her respective obligations under any VIE-related agreements (Guanyou Gamespace's breach of any of its obligations under the various VIE-related agreements will be treated as the shareholders' breach of their respective obligations), including the Equity Pledge Agreement, Gamespace is entitled to exercise its rights as the beneficiary under the Equity Pledge Agreement, including all the rights such shareholder has as a shareholder of Guanyou Gamespace.
- *Business Operation Agreement*, among Gamespace, Guanyou Gamespace and the shareholders of Guanyou Gamespace. This agreement sets forth the rights of Gamespace to control the actions of the shareholders of Guanyou Gamespace.
- *Powers of Attorney*, executed by the shareholders of Guanyou Gamespace in favor of Gamespace. These powers of attorney give Gamespace the exclusive right to appoint nominees to act on behalf of each of the two Guanyou Gamespace shareholders in connection with all actions to be taken by Guanyou Gamespace.
- *Technology Support and Utilization Agreement*, between Gamespace and Guanyou Gamespace. Pursuant to this agreement, Gamespace has the exclusive right to provide certain product development and application services and technology support to Guanyou Gamespace for a fee equal to a predetermined percentage of Guanyou Gamespace's revenues.
- *Services and Maintenance Agreement*, between Gamespace and Guanyou Gamespace. Pursuant to this agreement, Gamespace provides marketing, staffing, business operation and maintenance services to Guanyou Gamespace in exchange for a fee equal to the cost of providing such services plus a predetermined margin.

*Contractual Arrangements with Shanghai ICE and its Shareholders*

- *Exclusive Business Cooperation Agreement*, between ICE Information and Shanghai ICE. This agreement sets forth the exclusive right of ICE Information to provide business support and technical services to Shanghai ICE.
- *Exclusive Technology Consulting and Service Agreement*, between ICE Information and Shanghai ICE. Provides to ICE Information the exclusive right to provide technical consultation and other related services to Shanghai ICE in exchange for a fee equal to the balance of Shanghai ICE's gross income after deduction of related costs and expenses.
- *Business Operation Agreement*, among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE. This agreement sets forth the right of ICE Information to control the actions of the shareholders of Shanghai ICE.



- *Call Option Agreement*, among ICE Information, Shanghai ICE and Shanghai ICE shareholders. Provides to ICE Information and any third party designated by ICE Information the right, exercisable at any time during the term of the agreement, if and when it is legal to do so under PRC law, to purchase from the shareholders all or any part of their shares in Shanghai ICE or purchase from Shanghai ICE all or part of its assets or business at the lowest purchase price permissible under PRC law. The agreement further provides that Shanghai ICE or its shareholders will transfer back to ICE Information any such purchase price they have received from ICE Information, upon the request of ICE Information, as and to the extent allowed under PRC law.
- *Share Pledge Agreement*, among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE. Pledge by the shareholders to ICE Information of their equity interests in Shanghai ICE, to secure the performance of their obligations and Shanghai ICE's obligations under the various VIE-related agreements. If Shanghai ICE or any of the shareholders of Shanghai ICE breaches its, his or her obligations under any VIE-related agreements, ICE Information is entitled to exercise its rights as pledgee of the equity interests.

#### ***Transactions and Agreements with Sohu in connection with the carve-out of our MMOG Business from Sohu***

Expenses charged from Sohu for sales and marketing services and certain other services in connection with our business amounted to \$13.4 million, \$14.0 million and \$6.0 million, respectively, for the years ended December 31, 2013, 2012 and 2011. The amounts of these charges were agreed to by Sohu and us with reference to amounts charged for similar services by unrelated parties. Total corporate general administrative expenses allocated from Sohu were \$12,000, \$27,000 and \$1.5 million, respectively, for the years ended December 31, 2013, 2012 and 2011.

During the years from 2009 to 2013, we continued to use the Sohu logo, to purchase banner advertisements from Sohu, and, before our acquisition of the 17173 Business from Sohu on December 15, 2011, to pay Sohu to include advertisements for and links to our MMOGs on the 17173.com Website. For each of such banner advertisement and link placements, we paid Sohu at the same rates as Sohu charges third parties for such placements. We also used Sohu's PEAK online billing system and used Sohu to provide links to our MMOG Website on Sohu.com's main Website, for which we paid Sohu at a rate comparable to the rates charged by third-party providers for similar services and placements. In 2014, for so long as Sohu remains as our controlling shareholder, we intend to enter into new agreements, or make amendments to existing agreements, between us and Sohu that involve significant expenditures or commitments with reference to the terms of similar agreements between unrelated third parties. We will also submit such agreements and amendments for review by the audit committee of our Board of Directors, which will assess such agreements and amendments for potential conflicts of interest in accordance with the NASDAQ Listing Rules, and seek to ensure that terms of such agreements and amendments are no less favorable than would be comparable agreements between us and an unrelated third party. We have adopted a policy for our audit committee setting forth the guidelines under which related party transactions, including transactions between Sohu and us, must be reviewed and approved or ratified by the audit committee. In assessing a related party transaction, the audit committee is required to consider such factors as (i) the benefits to us of the transaction; (ii) the commercial reasonableness of the terms of the related party transaction; (iii) the materiality of the transaction to us; and (iv) the extent of the related party's interest in the transaction.

The following are summaries of a Master Transaction Agreement related to our carve-out from Sohu, an Amended and Restated Non-Competition Agreement, and an Amended and Restated Marketing Services Agreement between Sohu and us:

#### ***Master Transaction Agreement for Carve-out***

The Master Transaction Agreement with respect to our carve-out from Sohu contains key provisions relating to our carve-out from Sohu. The agreement provides for cross-indemnities that generally will place the financial responsibility on us for all liabilities associated with the current and historical MMORPG business and operations transferred to us, and generally will place on Sohu the financial responsibility for liabilities associated with all of Sohu's other current and historical businesses and operations, in each case regardless of the time those liabilities arise. The agreement also contains indemnification provisions under which we and Sohu indemnify each other with respect to breaches of the agreement or any related inter-company agreement.

In addition to our general indemnification obligations described above relating to the current and historical Sohu business and operations, we have agreed to indemnify Sohu against liabilities arising from misstatements or omissions in the prospectus for our initial public offering or the registration statement of which it is a part, except for misstatements or omissions relating to information that Sohu provided to us specifically for inclusion in the prospectus or the registration statement of which it forms a part. We also have agreed to indemnify Sohu against liabilities arising from any misstatements or omissions in our periodic SEC filings and from information we provide to Sohu specifically for inclusion in Sohu's annual or quarterly reports, but only to the extent that the information pertains to us or our business or to the extent Sohu provides us prior written notice that the information will be included in its annual or quarterly reports and the liability does not result from the action or inaction of Sohu.





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In addition to Sohu's general indemnification obligations described above relating to the current and historical Sohu business and operations, Sohu will indemnify us against liabilities arising from misstatements or omissions with respect to information that Sohu provided to us specifically for inclusion in the prospectus for our initial public offering or the registration statement of which it is a part. Sohu will also indemnify us against liabilities arising from information Sohu provides to us specifically for inclusion in our periodic SEC filings, but only to the extent that the information pertains to Sohu or Sohu's business or to the extent we provide Sohu prior written notice that the information will be included in our periodic SEC filings and the liability does not result from our action or inaction.

For liabilities arising from events occurring on or before April 1, 2009, the Master Transaction Agreement with respect to our carve-out from Sohu contains a general release. Under this provision, we release Sohu and its subsidiaries, VIEs, successors and assigns, and Sohu will release us and our subsidiaries, VIE, successors and assigns, from any liabilities arising from events between us on the one hand, and Sohu on the other hand, occurring on or before the date of the prospectus, including in connection with the activities to implement our initial public offering. The general release does not apply to liabilities allocated between the parties under the Master Transaction Agreement with respect to our carve-out from Sohu or the other inter-company agreements or to specified ongoing contractual arrangements.

Furthermore, under the Master Transaction Agreement with respect to our carve-out from Sohu, we have agreed to use our reasonable best efforts to use the same independent certified public accounting firm selected by Sohu and to maintain the same fiscal year as Sohu until such time as Sohu no longer owns at least a majority of our voting securities. We also have agreed to use our reasonable best efforts to complete our audit and provide Sohu with all financial and other information on a timely basis so that Sohu may meet its deadlines for its filing annual and quarterly financial statements.

#### *Amended and Restated Non-Competition Agreement*

We are a party to a Non-Competition Agreement, effective as of January 1, 2011 and amended and restated as of November 29, 2011, pursuant to which Sohu has agreed that, (i) until the later of three years after Sohu no longer owns in the aggregate at least 10% of the voting power of our then outstanding voting securities and March 17, 2014, or the general non-competition period, Sohu will not compete with us in the MMORPG business anywhere in the world, and (ii) until December 15, 2016, or the 17173 non-competition period, Sohu will not compete with us in the 17173 Business anywhere in the world, except that Sohu may, during the 17173 non-competition period, continue to own and operate a Web site through the domain name "games.sohu.com," for so long as content for and maintenance of such site is primarily provided by our staff. We have agreed during the general non-competition period not to compete with Sohu in the Internet portal, search, mobile value-added services and any other businesses conducted or contemplated to be conducted by Sohu as of April 1, 2009, except the MMORPG business and, after our acquisition of the 17173 Business on December 15, 2011, the 17173 Business. In addition, both parties have agreed not to solicit the employees of the other party.

#### *Amended and Restated Marketing Services Agreement*

We entered into a Marketing Services Agreement with Sohu, effective January 1, 2009, amended and restated as of January 1, 2010 and further amended as of January 1, 2011, pursuant to which Sohu provides certain rights and services to us, including marketing services and Sohu's PEAK system for the distribution of our virtual prepaid game cards. The agreement further provides for the license from Sohu to us of certain domain names, permits us to co-brand our games with the Sohu name and logos, and allows us to identify ourselves as a member of the Sohu Group. The agreement will terminate upon the later of the date that is three years after the first date upon which Sohu ceases to own in the aggregate at least 10% of the voting power of the then outstanding securities of Changyou and the fifth anniversary of March 17, 2009. The amendment and restatement of the Marketing Services Agreement effective January 1, 2010 includes certain amendments to the original agreement, including clarifications and rate adjustments, and terms under which Sohu provides us with space on Sohu servers for the purpose of our display on Sohu Websites of banner ads and promotional material, continues to give us rights to use the Sohu brand and logo, certain Sohu domain names, Sohu Passport and the Sohu PEAK online payment system, and provides certain services to us, such as the construction and maintenance of a bulletin board system for some of our MMOGs.

#### *Transaction Agreements for Our Purchase of the 17173 Business*

##### *17173 Transaction Agreement*

On November 29, 2011, we entered into a Master Transaction Agreement with Sohu respect to our acquisition of the 17173 Business, or the 17173 Transaction Agreement. Under the 17173 Transaction Agreement, we acquired from Sohu certain assets and business operations associated with the 17173 Business for fixed cash consideration of \$162.5 million. The parties agreed to customary representations, warranties, indemnities and covenants in the 17173 Transaction Agreement. Our acquisition of the 17173 Business closed on December 15, 2011. The 17173 Transaction Agreement provided for a brief transition period from December 16, 2011 through December 31, 2011, during which the net profits of \$1.3 million generated from our operation of the 17173 Business were for Sohu's benefit rather than ours.



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*Amended and Restated Non-Competition Agreement*

We and Sohu revised our existing non-competition agreement to provide Sohu's agreement not to compete with us in the 17173 Business for a period of five years following the closing of our acquisition of the 17173 Business and to remove the prior prohibition on our competing with Sohu in the 17173 Business. See "Major Shareholders and Related Party Transactions—Related Party Transactions—Transactions and Agreements with Sohu in connection with the carve-out of our MMORPG Business from Sohu—Amended and Restated Non-Competition Agreement" in Item 7 of this annual report.

*Services Agreement and Online Links and Advertising Agreement*

In addition, we and Sohu have entered into a services agreement and an online links and advertising agreement, referred to as the Services and Advertising Agreements, pursuant to which Sohu provides links and advertising space and technical support to us, including the provision and maintenance of user log-in, information management and virtual currency payment systems for the 17173 Business. The Services and Advertising Agreements provide for a term of twenty-five years for the virtual currency payment system services, and an initial term of three years for all the other services and links and advertising space, and involve aggregate fees payable by us to Sohu of approximately \$30 million. Under the Services and Advertising Agreements, we may renew certain rights for a subsequent term of twenty-two years, and may obtain a perpetual software license in respect of the information management system and the user log-in system following the expiration of the three-year term, subject to our payment to Sohu of additional fees of up to approximately \$5 million in the aggregate.

*Audit Committee and Board Approval of Our Acquisition of the 17173 Business*

Early in the course of discussions concerning a potential transaction regarding the 17173 Business between Sohu and us, we determined that, in view of Sohu's status as our controlling shareholder and Dr. Charles Zhang's positions as Chairman of the Board and Chief Executive Officer of Sohu as well as our Chairman of the Board, such a transaction would be a related party transaction, and we determined to (i) retain separate U.S. and PRC legal counsel to advise us on the proposed transaction, conduct legal due diligence on the 17173 Business and assist us with negotiation of the 17173 Transaction Agreement and related agreements and the Services and Advertising Agreements and (ii) retain a separate Big Four accounting firm to assist us with financial due diligence of the 17173 Business. In addition, our management asked the Audit Committee of our Board of Directors to separately consider the fairness to us of the consideration to be paid by us under the 17173 Transaction Agreement and to determine whether to recommend to our full Board of Directors that it approve the 17173 Transaction Agreement. Dr. Zhang recused himself from participation in the negotiation of the 17173 Transaction Agreement and the Services and Advertising Agreements, did not participate in discussion of such agreements and transactions by our Board of Directors and abstained from voting on such agreements and transactions on our Board of Directors.

We engaged a financial advisor in connection with the 17173 Transaction Agreement to render a fairness opinion to our Board of Directors that the consideration to be paid by Changyou under the 17173 Transaction Agreement is fair, from a financial point of view, to Changyou. Our Audit Committee of the Boards of Directors determined that the consideration to be paid by us was fair to Changyou and recommended that our full Board of Directors approve the 17173 Transaction Agreement. The full Board of Directors, in reliance upon the Audit Committee's recommendation and the fairness opinion of our financial advisor, determined that the consideration to be paid by Changyou was fair to Changyou and approved the 17173 Transaction Agreement.

The Audit Committee of our Board of Directors also recommended that our full Board of Directors approve the Services and Advertising Agreements, based on our management's report that the consideration under the Services and Advertising Agreements was determined based on prevailing market rates for similar services and links and advertising space. In addition, in reliance, in part, on such reports, our Audit Committee and our full Board of Directors determined that the consideration to be paid under the Services and Advertising Agreements was fair to us, and the Board of Directors approved the Services and Advertising Agreements.

*Amounts Due to/from Sohu*

Intercompany receivables from Sohu, arising mainly from customer advances collected by Sohu on our behalf, were \$0.4 million and \$0.5 million, respectively, as of December 31, 2013 and 2012. Prepaid expenses and non-current assets recorded in relation to services and advertising agreements we entered into with Sohu were \$10.4 million as of December 31, 2013, compared to \$20.2 million as of December 31, 2012. These balances are interest free and settleable on demand, and are measured at the amount of consideration established and agreed to by the related parties, which approximates amounts that would be charged to third parties.

*Amounts Due to/from Chong Qing Zhong Ying Jin Dian Cinema Co., Ltd and Shi Dai Jin Dian Cinema Investing Co., Ltd ("Jin Dian")*

Intercompany payables to Jin Dian, arising mainly from our purchasing exclusive rights to place advertisements in pre-film screening cinema advertising slots in Jin Dian's movie theatres, were \$3.1 million as of September 27, 2013, compared to \$4.2 million as of December 31, 2012. Jin Dian is controlled by Mr. Baoquan Zhang, who was a member of our Board of Directors until his resignation on September 27, 2013. Jin Dian was no longer considered to be our related party after Mr. Zhang's resignation.



***Amounts Due to/from Shenzhen Zhou You Network Technology Ltd (“Zhou You”)***

In January 2010, AmazGame acquired 30% of the equity interests in Zhou You and we have significant influence over Zhou You. As of December 31, 2013, intercompany payables to Zhou You were \$0.3 million, arising mainly from royalty fees paid to Zhou You for a licensed game, compared to \$0.3 million as of December 31, 2012.

***Interests of Experts and Counsel***

Not applicable.

**ITEM 8. FINANCIAL INFORMATION**

***Consolidated Financial Statements***

Please see Item 18 “Financial Statements” for our audited consolidated financial statements filed as a part of this annual report.

***Legal Proceedings***

We may be subject to legal proceedings, investigations and claims incidental to the conduct of our business from time to time. We are not currently a party to, nor are we aware of, any legal proceeding, investigation or claim which, in the opinion of our management, is likely to have a material adverse effect on our business, financial condition or results of operations.

***Dividend Policy***

In 2011 and 2013, we did not declare or pay any dividends. In August 2012, our Board of Directors declared a special one-time cash dividend of \$1.90 per Class A ordinary shares or Class B ordinary share, or \$3.80 per ADS (each representing two Class A ordinary shares). The total amount of the special cash dividend was approximately \$200.9 million. In order to expedite the payment of the special cash dividend, we financed the payment through loans from offshore banks which are secured by an equivalent amount of RMB-denominated onshore bank deposits of our subsidiaries in China. The dividend was paid to our shareholders on September 21, 2012.

Future cash dividends, if any, will be declared at the sole discretion of our Board of Directors and will depend upon our future operations and earnings, capital requirements and surplus, general financial condition, contractual restrictions and other factors as our Board of Directors may deem relevant.

Holders of ADSs will be entitled to receive dividends, subject to the terms of the deposit agreement, to the same extent as the holders of our ordinary shares, less the fees and expenses payable under the deposit agreement. Cash dividends will be paid by the depositary to holders of ADSs in U.S. dollars, subject to the terms of the deposit agreement. Other distributions, if any, will be paid by the depositary to holders of ADSs in any means it deems legal, fair and practical.



## ITEM 9. THE OFFER AND LISTING

Our ADSs are listed on the NASDAQ Global Select Market under the symbol “CYOU.” Trading in our ADSs commenced on April 2, 2009.

The following table provides the high and low reported sale prices for our ADSs on the NASDAQ Global Select Market for (1) each quarter in the two most recent fiscal years, (2) the last five months in the two most recent fiscal years and (3) the most recent quarters.

	Trading Price (\$)	
	High	Low
<b>2012</b>		
Full Year	29.52	17.00
First Quarter	29.52	21.77
Second Quarter	28.87	20.12
Third Quarter	27.74	17.00
Fourth Quarter	27.32	22.49
<b>2013</b>		
Full Year	41.64	26.52
First Quarter	32.90	26.64
Second Quarter	32.49	27.07
Third Quarter	36.67	27.72
Fourth Quarter	41.64	26.52
August	33.55	27.72
September	36.67	28.21
October	41.64	27.51
November	29.98	26.52
December	32.09	27.34
<b>2014</b>		
January	34.32	28.60
February (through February 21, 2014)	30.60	25.00

## ITEM 10. ADDITIONAL INFORMATION

### *Memorandum and Articles of Association*

We incorporate by reference into this annual report the description of our second amended and restated memorandum of association contained in our Registration Statement on Form F-1 (File No. 333-158061) originally filed with the SEC on March 17, 2009. Our shareholders adopted our second amended and restated memorandum and articles of association by a special resolution on March 16, 2009.

### *Differences in Corporate Law - Mergers and Similar Arrangements*

Set forth below is a summary of the significant differences between the provisions of the Companies Law Cap. 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands (the “Companies Law”) regarding mergers and similar arrangements that are applicable to us and the laws applicable to companies incorporated in the United States and their shareholders.

Under the laws of the Cayman Islands, two or more companies may merge or consolidate in accordance with Part XVI of the Companies Law. Merger means the merging of two or more constituent companies into a sole remaining constituent company or surviving company and the vesting of the undertaking, property and liabilities of the constituent companies in the surviving company. Consolidation means the combination of two or more constituent companies into a new consolidated company and the vesting of the undertaking, property and liabilities of the constituent companies in the consolidated company. The directors of each constituent company must approve a written plan of merger or consolidation (the “Plan”). The Plan must contain certain prescribed information including the effective date of the merger or consolidation; the basis of cancelling the shares in a constituent company in exchange for the relevant consideration or converting the shares in each constituent company into shares of the consolidated company or surviving company and the rights attached thereto; any proposed amendments to the memorandum and articles of association of the surviving company in a merger or the proposed new memorandum and articles of association of the consolidated company in a consolidation; and details of all secured creditors.



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The Plan must be approved by each constituent company by way of (a) a special resolution of the shareholders; and (b) such other authorization, if any, as may be specified in such constituent company's articles of association. Shareholders do not need to approve a merger between a Cayman Islands parent company and a Cayman Islands subsidiary. For this purpose a subsidiary is a company of which at least 90% of the issued shares entitled to vote are owned by the parent company.

The consent of each holder of a fixed or floating security interest over a constituent company is required unless this requirement is waived by a court in the Cayman Islands.

The Plan must be filed with the Registrar of Companies together with supporting documents including a declaration (a) of solvency (debts as they fall due); (b) that the merger or consolidation is bona fide and not intended to defraud unsecured creditors of the constituent companies; (c) of the assets and liabilities of each constituent company; (d) that no proceedings are outstanding and that no order has been made or resolution passed to wind up a constituent company or to appoint a receiver, trustee or administrator in any jurisdiction; (e) that no scheme, order, compromise or arrangement has been made in any jurisdiction whereby the rights of creditors have been suspended or restricted and an undertaking that a copy of the certificate of merger or consolidation will be given to members and creditors of the constituent company and notification of the merger or consolidation will be published in the Cayman Islands Gazette.

A certificate of merger or consolidation, which is prima facie evidence of compliance with all statutory requirements in respect of the merger or consolidation, is issued by the Registrar of Companies.

The effective date of a merger or consolidation is the date the Plan is registered by the Registrar of Companies, although the Plan may provide for an effective date up to 90 days after the date of registration.

Except under certain circumstances a dissenting shareholder of a Cayman Islands constituent company is entitled to payment of the fair value of his shares upon dissenting to a merger or consolidation. The exercise of appraisal rights will preclude the exercise of any other rights except for the right to seek relief on the grounds that the merger or consolidation is void or unlawful.

The following procedure will otherwise apply:

- The dissenting shareholder must give written notice of objection ("notice of objection") to the constituent company before the vote to approve the merger or consolidation.
- Within 20 days of the vote approving the merger or consolidation the constituent company must give written notice of the approval ("approval notice") to all dissenting shareholders who served a notice of objection.
- Within 20 days ("dissent period") of the approval notice a dissenting shareholder must give a written notice of dissent ("notice of dissent") to the constituent company demanding payment of the fair value of his shares.
- Within 7 days of the expiry of the dissent period or within 7 days of the date on which the plan of merger or consolidation is filed with the Registrar of Companies (whichever is later) the constituent company, surviving company or consolidated company must make a written offer ("fair value offer"), to each dissenting shareholder to purchase their shares at a price determined by the company to be their fair value.
- If the company and the dissenting shareholders fail to agree the price within 30 days of the fair value offer ("negotiation period"), then within 20 days of the expiry of the negotiation period the company must apply to the Grand Court of the Cayman Islands to determine the fair value of the shares held by all dissenting shareholders who have served a notice of dissent and who have not agreed the fair value with the company.

All rights, benefits, immunities, privileges and property (including business and goodwill) of each of the constituent companies will vest in the surviving or consolidated company which will be liable for all debts, contracts, obligations, mortgages, charges, security interests and liabilities of each constituent company. Existing claims, proceedings, judgments, orders or rulings applicable to each constituent company will automatically apply to the surviving company or the consolidated company.

In addition, there are statutory provisions that facilitate the reconstruction and amalgamation of companies, provided that the scheme of arrangement is approved by a majority in number of each class of shareholders and creditors with whom the arrangement is to be made, and who must in addition represent three-fourths in value of each such class of shareholders or creditors, as the case may be, that are present and voting either in person or by proxy at a meeting, or meetings, convened for that purpose by order of the Grand Court of the Cayman Islands. The arrangement must be sanctioned by the Grand Court of the Cayman Islands. While a dissenting shareholder has the right to express to the court the view that the transaction ought not to be approved, the court can be expected to approve the arrangement if it determines that:

- the statutory provisions as to the required vote have been met;
- the shareholders have been fairly represented at the meeting in question and the statutory majority are acting bona fide without coercion of the minority;





- the arrangement is such that may be reasonably approved by an intelligent and honest man acting in respect of his interest in the relevant class; and
- the arrangement is not one that would more properly be sanctioned under some other provision of the Companies Law.

When a take-over offer is made for all the shares or all the shares of a particular class and accepted by holders of 90% of the shares which are the subject of the offer within four months of the date of the offer, the offeror may, within a two month period commencing on the expiration of such four month period, require the holders of the remaining shares to transfer their shares on the terms of the offer. An objection can be made to the Grand Court of the Cayman Islands but this is unlikely to succeed in the case of an offer which has been so approved unless there is evidence of fraud, bad faith, or breach of the Companies Law.

If a scheme of arrangement or take-over offer is approved or accepted, the dissenting shareholder(s) are unlikely to have any rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of United States corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

### *Material Contracts*

We have not entered into any material contracts within the past two fiscal years other than in the ordinary course of business, other than those listed in Item 19 “Exhibits” or described elsewhere in this annual report, or as described below.

### *Purchase of Office Building*

On August 23, 2010, we entered into an agreement with a property developer to purchase an office building to be built in Beijing at a price of approximately \$162.4 million to serve as our headquarters. The agreement provides for the developer to start construction in the first half of 2011, subject to necessary permits’ being obtained, and specifies that the developer was expected to complete construction and deliver the building to us by the end of 2012. The agreement states that building was expected to have an office and ancillary area of approximately 56,200 square meters. Since the area of the premises had not been pre-measured at the time of the signing of the Agreement, the area and the price contained in the agreement were estimates. The developer obtained an advance sale permit for the project in December 2011, which under PRC law allows the developer to sell the building to us in advance, before construction is completed. We then entered into an advance sale contract with respect to the purchase, specifying that the building was expected to have an area of approximately 56,549 square meters and that we were expected to pay up to 90% of the total purchase price to the developer upon the developer’s certifying completion of the building. Under the August 23, 2010 agreement and the advance sale contract, the remaining balance of the purchase price is to be adjusted based on the actual floor area built, the final unit price agreed to by the parties and cost adjustments, which have been agreed to be approximately \$3.2 million, related to changes to the original design of the building. The developer certified completion of the building in January 2013. We had paid \$165.2 million through December 31, 2013 pursuant to the August 23, 2010 agreement and the advance sale contract. Depreciation of the building commenced in January 2014.

### *Amended and Restated Market Services Agreement with Sohu*

Please refer to “Related Party Transactions—Transactions and Agreements with Sohu in connection with the carve-out of our MMORPG Business from Sohu” in Item 7 of this annual report.

### *7Road Transactions*

#### *Share Transfer Framework Agreement with 7Road*

On April 22, 2011, we entered into a Share Transfer Framework Agreement under which we, through our subsidiaries and Gamease, one of our VIEs, acquired 68.258% of the equity interests in Shenzhen 7Road, which is engaged in Web game operation (through third-party joint operators) and development in China. The purchase price consists of fixed cash consideration of approximately \$68.26 million and additional variable cash consideration of up to a maximum of \$32.76 million, contingent upon the achievement by 7Road of specified performance milestones through December 31, 2012. On and after the closing, four of the then shareholders of Shenzhen 7Road, who are also existing members of management of 7Road, or 7Road management shareholders, continued to hold 31.742% of the equity interests in Shenzhen 7Road and each entered into an employment agreement and a non-competition agreement with Shenzhen 7Road. Under the Share Transfer Framework Agreement, we have the right to designate three of the five directors of 7Road, including the chairman of the board. Also under the Share Transfer Framework Agreement, if 7Road achieves specified performance milestones through December 31, 2013 but there has not been an initial public offering for 7Road, then the 7Road management shareholders will have a right to sell all or a portion of their equity interests in 7Road to us, at a price determined based on 7Road’s net income. We completed the acquisition under the Share Transfer Framework Agreement on May 11, 2011. We completed the 7Road Reorganization, which was contemplated by the Share Transfer Framework Agreement, on June 26, 2012.



See “Information on the Company—History and Development of the Company” in Item 4 of this annual report.

#### *Acquisition Framework Agreement*

On May 1, 2013, we entered into an Acquisition Framework Agreement pursuant which we acquired all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders and through our VIE Gamease, all of the equity interests in Shenzhen 7Road held by shareholders other than Gamease, for aggregate cash consideration of approximately \$78 million. Effective with our entering into the agreement, Mr. Dewen Chen, Changyou’s President, was appointed as the Chairman and Chief Executive Officer of 7Road. As a result of the acquisition, which was completed on June 5, 2013, 7Road became our indirect wholly-owned subsidiary and our VIE Gamease became the sole shareholder of our VIE Shenzhen 7Road. Also effective upon the closing of the acquisition, the former non-controlling shareholders’ existing non-compete covenants with us were terminated, and an agreement took effect under which the former non-controlling shareholders agreed, for a period of two years after the closing, to not solicit or hire existing employees of 7Road.

#### *Transaction Agreements with Kalends Group*

##### *Investment Agreement*

On November 19, 2013, we, through our indirect wholly-owned subsidiary Heroic, entered into an investment agreement with the Kalends Group. See “Information on the Company—History and Development of the Company” in Item 4 of this annual report.

##### *Shareholder Agreement*

In connection with the investment agreement, Heroic, the Kalends Group and TalkTalk entered into a shareholder agreement, effective upon the closing under the investment agreement on December 24, 2013, pursuant to which we will have the right to designate three of the five directors of TalkTalk, including the chairman of the board, and we will have customary rights of first refusal with respect to proposed transfers of equity interests in TalkTalk by the Kalends Group. The shareholder agreement also specifies that if TalkTalk fails to achieve specified performance milestones for the month of December 2014, then the Kalends Group, any key employees of TalkTalk who hold equity interests in TalkTalk, and, under certain circumstances, TalkTalk will be required to issue to us, without consideration, equity interests in TalkTalk in amounts sufficient to cause our equity interest to increase to 70% on a fully-diluted basis.

#### *Exchange Controls*

China’s government imposes control over the convertibility of RMB into foreign currencies. The conversion of RMB into foreign currencies, including U.S. dollars, has been based on rates announced by the People’s Bank of China. 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. This change in policy has resulted in an approximately 0.25% appreciation of the RMB against the U.S. dollar by the end of 2013. While the international reaction to the RMB revaluation has generally been positive, there remains significant international pressure on the PRC government to adopt an even more flexible currency policy, which could result in a further and more significant appreciation of the RMB against the U.S. dollar.

Pursuant to the Foreign Exchange Administration Regulations issued by the State Council on January 29, 1996, and effective as of April 1, 1996 (and amended on January 14, 1997 and August 5, 2008) and the Regulations on the Administration of Settlement, Sale and Payment of Foreign Exchange issued by the People’s Bank of China on June 20, 1996 and effective on July 1, 1996, or the FX Regulations, regarding the administration and control of foreign exchange, conversion of RMB into foreign exchange by foreign investment enterprises for current account items, including the distribution of dividends and profits to foreign investors of joint ventures, is permissible. Foreign investment enterprises are permitted to remit foreign exchange from their foreign exchange bank account in China on the basis of, inter alia, the terms of the relevant joint venture contracts and the board resolutions declaring the distribution of the dividend and payment of profits. On January 14, 1997, the State Council amended the Foreign Exchange Administration Regulations and added, among other things, an important provision, as Article 5 provides that the State shall not impose restrictions on recurring international current account payments and transfers. Conversion of RMB into foreign currencies and remittance of foreign currencies for capital account items, including direct investment, loans, security investment, is still subject to the approval of the SAFE, in each such transaction.

Under the Foreign Exchange Administration Regulations, foreign investment enterprises are required to open and maintain separate foreign exchange accounts for capital account items (but not for other items). In addition, foreign investment enterprises may only buy, sell and/or remit foreign currencies at those banks authorized to conduct foreign exchange business upon the production of valid commercial documents and, in the case of capital account item transactions, document approval from the SAFE.



Currently, foreign investment enterprises are required to apply to the SAFE for “foreign exchange registration certificates for foreign investment enterprises” (which are granted to foreign investment enterprises, upon fulfilling specified conditions and which are subject to review and renewal by the SAFE on an annual basis). With such foreign exchange registration certificates and required underlying transaction documents, or with approval documents from the SAFE if the transactions are under capital account (which are obtained on a transaction-by-transaction basis), foreign-invested enterprises may enter into foreign exchange transactions at banks authorized to conduct foreign exchange business to obtain foreign exchange for their needs.

## **Taxation**

*The following summary of the material Cayman Islands, PRC and United States federal income tax consequences of an investment in our ADSs or Class A ordinary shares is based upon laws and relevant interpretations thereof in effect as of the date of this annual report, all of which are subject to change. This summary does not discuss all possible tax consequences relating to an investment in our ADSs or Class A ordinary shares, such as the tax consequences under United States state, local and other tax laws.*

### **Cayman Islands Taxation**

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciation and there is no taxation in the nature of inheritance tax or estate duty. There are no other taxes likely to be material to us levied by the Government of the Cayman Islands except for stamp duties which may be applicable on instruments executed in, or brought within the jurisdiction of the Cayman Islands. The Cayman Islands is not party to any double tax treaties. There are no exchange control regulations or currency restrictions in the Cayman Islands.

### **PRC Taxation**

#### ***PRC taxation of us and our corporate group***

We are a holding company incorporated in the Cayman Islands and hold our equity interests in AmazGame, 7Road Technology, Gamespace, ICE Information and Changyou Raidcall, our PRC subsidiaries, indirectly through Changyou HK, 7Road HK and ICE HK, our Hong Kong subsidiaries. A significant portion of our business operations are conducted by these PRC subsidiaries through our VIEs Gamease, Shenzhen 7Road, Guanyou Gamespace and Shanghai ICE. The CIT Law and its implementation rules provide that China-sourced income of foreign enterprises, such as dividends paid by a PRC subsidiary to its overseas parent that is not a PRC resident enterprise and has no establishment in the PRC, will normally be subject to PRC withholding tax at a rate of 10%, unless there are applicable tax treaties that reduce such rate. Under the China-HK Tax Arrangement, such dividend withholding tax rate may be reduced to 5% if a Hong Kong resident enterprise is considered a non-PRC tax resident enterprise and owns at least 25% of equity interests in the PRC company distributing the dividends, subject to approval of the PRC local tax authority. However, if the Hong Kong resident enterprise is not considered to be the beneficial owner of such dividends under applicable PRC tax regulations, such dividends may remain subject to withholding tax at a rate of 10%. On October 27, 2009, the SAT issued Circular 601, which provides guidance on determining whether an enterprise is a “beneficial owner” under China’s tax treaties and tax arrangements. Circular 601 Circular provides that, in order to be a beneficial owner, an entity generally must be engaged in substantive business activities, and that a company that is set up for the purpose of avoiding or reducing taxes or transferring or accumulating profits, will not be regarded as a beneficial owner and will not qualify for treaty benefits such as preferential dividend withholding tax rates. If any of our Hong Kong subsidiaries is, in the light of Circular 601, considered to be a non-beneficial owner for purposes of the China-HK Tax Arrangement, any dividends paid to it by any of our PRC subsidiaries would not qualify for the preferential dividend withholding tax rate of 5%, but rather would be subject to withholding tax at the usual CIT Law rate of 10%.

Under the CIT Law, enterprises established under the laws of jurisdictions outside China with their “de facto management bodies” located within China may be considered to be PRC tax resident enterprises for tax purposes. A substantial majority of the members of our management team as well as the management team of Changyou HK, 7Road HK and ICE HK are located in China. If we, Changyou HK, 7Road HK or ICE HK is considered a PRC tax resident enterprise under the above definition, then our global income will be subject to PRC enterprise income tax at the rate of 25%.

#### ***PRC taxation of our overseas shareholders***

The implementation rules of the CIT Law provide that, (i) if the enterprise that distributes dividends is domiciled in the PRC, or (ii) if gains are realized from transferring equity interests of enterprises domiciled in the PRC, then such dividends or capital gains are treated as China-sourced income. It is not clear how “domicile” may be interpreted under the CIT Law, and it may be interpreted as the jurisdiction where the enterprise is a tax resident. Therefore, if we and Changyou HK are considered as a PRC tax resident enterprise for tax purposes, any dividends we pay to our overseas shareholders or ADS holders as well as gains realized by such shareholders or ADS holders from the transfer of our shares or ADSs may be regarded as China-sourced income and as a result become subject to PRC withholding tax at the rate up to 10%. See “Risk Factors—There are significant uncertainties under the new corporate income tax law of the PRC, or the CIT Law, regarding our PRC enterprise income tax liabilities, such as tax on dividends paid to us by our PRC subsidiary. The CIT Law also contains uncertainties regarding possible PRC withholding tax on any dividends we pay to our overseas corporate shareholders and gains realized from the transfer of our shares by our overseas corporate shareholders.”



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*United States Federal Income Taxation*

The following is a general summary of the material United States federal income tax considerations related to the purchase, ownership and disposition of our ADSs or Class A ordinary shares by U.S. holders (as defined below). This summary applies only to U.S. holders that hold the ADSs or Class A ordinary shares as capital assets and that have the U.S. dollar as their functional currency. This discussion is based on the tax laws of the United States as in effect on the date of this annual report and on United States Treasury regulations in effect or, in some cases, proposed, as of the date of this annual report, as well as judicial and administrative interpretations thereof available on or before such date. All of the foregoing authorities are subject to change, which change could apply retroactively and could affect the tax consequences described below.

The following discussion does not describe all of the tax consequences that may be relevant to any particular investor or to persons in special tax situations such as:

- certain financial institutions;
- insurance companies;
- broker dealers;
- traders that elect to mark to market;
- tax-exempt entities;
- persons liable for alternative minimum tax;
- persons holding ADSs or Class A ordinary shares as part of a straddle, hedging, conversion or integrated transaction;
- persons that actually or constructively own 10% or more of our voting shares; or
- persons holding ADSs or Class A ordinary shares through partnerships or other pass-through entities.

*U.S. holders are urged to consult their tax advisors about the application of the United States federal tax rules to their particular circumstances as well as the state, local and foreign tax consequences to them of the purchase, ownership and disposition of ADSs or Class A ordinary shares.*

The discussion below of the United States federal income tax consequences to “U.S. holders” will apply to a beneficial owner of ADSs or Class A ordinary shares who is, for United States federal income tax purposes:

- a citizen or individual resident of the United States;
- a corporation (or other entity taxable as a corporation for United States federal income tax purposes) organized under the laws of the United States, any state or the District of Columbia;
- an estate whose income is subject to United States federal income taxation regardless of its source; or
- a trust that (1) is subject to the supervision of a court within the United States and the control of one or more United States persons or (2) has a valid election in effect under applicable United States Treasury regulations to be treated as a United States person.

The tax treatment of a partner in a partnership or other entity taxable as a partnership that holds ADSs or Class A ordinary shares, depends on the partner’s status and the activities of the partnership. U.S. holders that hold their ADSs or Class A ordinary shares through a partnership, limited liability company, or other entity taxable as a partnership should consult their tax advisers regarding their tax treatment.

The discussion below assumes that the representations contained in the Deposit Agreement are true and that the obligations in the Deposit Agreement and any related agreement will be complied with in accordance with their terms. Holders of ADSs will be treated as the holders of the underlying Class A ordinary shares represented by those ADSs for United States federal income tax purposes. Accordingly, deposits of Class A ordinary shares in return for ADSs representing those shares, and surrender of ADSs in return for the underlying Class A ordinary shares, will not be subject to United States federal income tax.



### ***Taxation of Dividends and Other Distributions on ADSs or Class A Ordinary Shares***

Subject to the passive foreign investment company rules discussed below, the gross amount of our distributions to a U.S. holder with respect to ADSs or Class A ordinary shares (including any amount withheld in respect of PRC taxes) generally will be included in a U.S. holder's gross income as foreign source dividend income on the date of receipt by the depositary, in the case of ADSs, or by the U.S. holder, in the case of Class A ordinary shares, but only to the extent that the distribution is paid out of our current or accumulated earnings and profits (as determined under United States federal income tax principles). To the extent, if any, that the amount of any such distribution exceeds our current and accumulated earnings and profits, it will be treated first as a tax-free return of the U.S. holder's tax basis in the ADSs or the Class A ordinary shares (thereby increasing the amount of any gain or decreasing the amount of any loss realized on the subsequent sale or disposition of such ADSs or Class A ordinary shares) and thereafter as capital gain. U.S. holders should note that we do not intend to calculate our earnings and profits under United States federal income tax principles. Therefore, a U.S. holder should expect that a distribution generally will be reported as a dividend even if that distribution should be treated as a non-taxable return of capital or as capital gain under the rules described above. Further, the dividends will not be eligible for the dividends-received deduction allowed to corporations in respect of dividends received from other United States corporations.

With respect to certain non-corporate U.S. holders, including individual U.S. holders, dividends may be taxed at a special rate (the applicable capital gains rate) that is applicable to "qualified dividend income" provided that (1) the ADSs or Class A ordinary shares are readily tradable on an established securities market in the United States, (2) we are not treated as a passive foreign investment company with respect to the U.S. holder (as discussed below) for our taxable year in which the dividend was paid and we were not a passive foreign investment company in the preceding taxable year, and (3) certain holding period requirements are met. Under Internal Revenue Service authority, our Class A ordinary shares, or ADSs representing such shares, will be considered for the purpose of clause (1) above to be readily tradable on an established securities market in the United States if they are listed (as our ADSs currently are) on the NASDAQ Global Select Market. U.S. holders should consult their tax advisors regarding the availability of the lower rate for dividends paid with respect to our ADSs or Class A ordinary shares. For foreign tax credit purposes, dividends paid on our Class A ordinary shares will generally constitute "passive category income" but could, in the case of certain U.S. holders, constitute "general category income."

If PRC withholding taxes apply to dividends paid to a U.S. holder with respect to our ADSs or Class A ordinary shares, subject to certain conditions and limitations, such PRC withholding taxes will be treated as foreign taxes eligible for credit against the U.S. holder's United States federal income tax liability. The rules governing foreign tax credits are complex and, therefore, U.S. holders should consult their tax advisors regarding the availability of a foreign tax credit in such U.S. holders' particular circumstances.

### ***Taxation of Disposition of Shares***

Subject to the passive foreign investment company rules discussed below, a U.S. holder will recognize taxable gain or loss on any sale, exchange or other taxable disposition of an ADS or Class A ordinary share equal to the difference between the amount realized for the ADS or Class A ordinary share and the U.S. holder's tax basis in the ADS or Class A ordinary share. The gain or loss will be capital gain or loss. A non-corporate U.S. holder, including an individual U.S. holder, who has held the ADS or Class A ordinary share for more than one year will be eligible for reduced capital gains tax rates. The deductibility of capital losses is subject to limitations. Any such gain or loss that a U.S. holder recognizes will be treated as United States source income (or loss, in the case of losses, subject to certain limitations).

As described above under "Taxation—PRC Taxation," any gain from the disposition of our ADSs or Class A ordinary shares may be subject to PRC withholding tax. In such event, a U.S. holder that is eligible for the benefits of the income tax treaty between the United States and the PRC may elect to treat the gain as PRC source income for foreign tax credit purposes. U.S. holders should consult their tax advisors regarding their eligibility for benefits under the income tax treaty between the United States and the PRC and their ability to credit any PRC tax withheld in respect of a sale of our ADSs or Class A ordinary shares against their United States federal income tax liability.





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*Passive Foreign Investment Company*

We believe that we will not be treated as a passive foreign investment company (“PFIC”) for U.S. federal income tax purposes for our taxable year ending November 30, 2013. Our expectation is based on our current and anticipated operations and composition of our earnings and assets for the 2013 taxable year, including the current and expected valuation of our assets (including goodwill) based on the expected price of our ADSs in the market. However, because we currently hold, and expect to continue to hold a substantial amount of cash, and because the value of our other assets may be based in part on the market price of our ADSs, which has fluctuated and is likely to continue to fluctuate (and may fluctuate considerably given that market prices of Internet and online game companies historically have been especially volatile), our PFIC status may depend in large part on the market price of our ADSs. Accordingly, fluctuations in the market price of our ADSs may result in our being a PFIC for any taxable year. In addition, the composition of our income and assets will be affected by how, and how quickly, we spend our cash. Furthermore, it is not entirely clear how the contractual arrangements between us and our consolidated VIEs will be treated for purposes of the PFIC rules. If these contractual arrangements were found by PRC authorities with appropriate jurisdiction to be unenforceable, this could cause more than 75% of our gross income or more than 50% of our assets to be passive in the year that this finding was made or in subsequent years, which could cause us to be classified as a PFIC. See “Risk Factors—Risks Related to Our Corporate Structure and PRC Law and Regulations—Our contractual arrangements with our VIEs and their shareholders may not be as effective in providing control over our VIEs as direct ownership of the VIEs and the shareholders of our VIEs may have conflicts of interest with us or with each other.” Also our actual PFIC status for any taxable year will depend upon the character of our income and assets and the value of our assets for such year, which will not be determinable until after the close of the taxable year. Accordingly, there is no guarantee that we will not be a PFIC for any taxable year.



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A non-U.S. corporation is considered a PFIC for any taxable year if either:

- at least 75% of its gross income is passive income (the “income test”), or
- at least 50% of the value of its assets (based on an average of the quarterly values of the assets during a taxable year) is attributable to assets that produce or are held for the production of passive income (the “asset test”).

For the purposes of this determination, we will be treated as owning our proportionate share of the assets and earning our proportionate share of the income of any other corporation in which we own, directly or indirectly, at least 25% (by value) of the shares.

We must make a separate determination each year as to whether we are a PFIC. As a result, our PFIC status may change.

If we are a PFIC for any taxable year during which a U.S. holder holds ADSs or Class A ordinary shares, such U.S. holder will be subject to special tax rules with respect to any “excess distribution” that such U.S. holder receives and any gain that such U.S. holder realizes from a sale or other disposition (including a pledge) of the ADSs or Class A ordinary shares, unless the holder makes a “mark-to-market” election as discussed below. For purpose of these special rules, if we are a PFIC for any year during which a U.S. holder holds ADSs or Class A ordinary shares, we will continue to be treated as a PFIC with respect to such U.S. holder for all succeeding years during which such U.S. holder holds ADSs or Class A ordinary shares. Under certain attribution rules, if we are a PFIC, a U.S. holder will be deemed to own such U.S. holder’s proportionate share of any subsidiaries or other entities that are PFICs in which we hold (directly or indirectly through other PFICs) an equity interest (“subsidiary PFICs”), and will generally be treated for purposes of the PFIC rules as if such U.S. holder directly held the shares of such subsidiary PFICs.

Under these special rules, distributions that a U.S. holder receives in a taxable year that are greater than 125% of the average annual distributions that such U.S. holder received during the shorter of the three preceding taxable years or such U.S. holder’s holding period for the ADSs or Class A ordinary shares will be treated as an excess distribution. Under these special tax rules:

- the excess distribution or gain will be allocated ratably over the U.S. holder’s holding period for the ADSs or Class A ordinary shares;
- the amount allocated to the current taxable year, and any taxable year prior to the first taxable year in which we became a PFIC, will be treated as ordinary income; and
- the amount allocated to each other taxable year will be subject to the highest tax rate in effect for that taxable year and the interest charge generally applicable to underpayments of tax will be imposed on the resulting tax attributable to each such taxable year.

The tax liability for amounts allocated to years prior to the year of disposition or “excess distribution” cannot be offset by any net operating losses for such years, and gains (but not losses) realized on the sale of ADSs or Class A ordinary shares cannot be treated as capital, even if the U.S. holder holds the ADSs or Class A ordinary shares as capital assets. A U.S. holder will be subject to the same United States federal income tax rules as described above on indirect or constructive distributions that the U.S. holder is deemed to receive on shares of a subsidiary PFIC and on indirect or constructive dispositions of shares of subsidiary PFICs.

Alternatively, a U.S. holder of “marketable stock” (as defined below) in a PFIC may make a mark-to-market election for such stock of a PFIC to elect out of the tax treatment discussed in the two preceding paragraphs. A mark-to-market election will not be available, however, with respect to any subsidiary PFICs. If a U.S. holder makes a mark-to-market election for the ADSs or Class A ordinary shares, such U.S. holder will include in income each year an amount equal to the excess, if any, of the fair market value of the ADSs or Class A ordinary shares as of the close of such U.S. holder’s taxable year over such U.S. holder’s adjusted basis in such ADSs or Class A ordinary shares. The U.S. holder will be allowed a deduction for the excess, if any, of the adjusted basis of the ADSs or Class A ordinary shares over their fair market value as of the close of the taxable year. However, deductions are allowable only to the extent of any net mark-to-market gains on the ADSs or Class A ordinary shares included in the U.S. holder’s income for prior taxable years. Amounts included in a U.S. holder’s income under a mark-to-market election, as well as gain on the actual sale or other disposition of the ADSs or Class A ordinary shares, will be treated as ordinary income. Ordinary loss treatment will also apply to the deductible portion of any mark-to-market loss on the ADSs or Class A ordinary shares, as well as to any loss realized on the actual sale or disposition of the ADSs or Class A ordinary shares, to the extent that the amount of such loss does not exceed the net mark-to-market gains previously included for such ADSs or Class A ordinary shares. A U.S. holder’s basis in the ADSs or Class A ordinary shares will be adjusted to reflect any such income or loss amounts. If the U.S. holder makes a mark-to-market election, tax rules that apply to distributions by corporations which are not PFICs would apply to distributions by us (except that the lower applicable capital gains rate for “qualified dividend income” discussed above would not apply). The basis adjustment and income or loss inclusion described here under this alternate mark-to-market regime will only apply during years in which we are a PFIC.



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The mark-to-market election will only be available for “marketable stock” which is stock that is traded in more than de minimis quantities on at least 15 days during each calendar quarter on a qualified exchange or other market, as defined in applicable Treasury regulations. We expect that the ADSs will continue to be listed and regularly traded on the NASDAQ Global Select Market, which is a qualified exchange for these purposes, and, consequently, it can be expected that the mark-to-market election would be available to U.S. holders of our ADSs if we were to become a PFIC.

A third alternative taxation regime which may be available to some U.S. investors in PFICs, known as “qualified electing fund” (QEF) treatment, will not be available to U.S. holders of our ADSs or Class A ordinary shares. This is because QEF treatment requires the PFIC to supply annually certain information to U.S. holders of ADSs or Class A ordinary shares, and we will not be supplying such information.

A U.S. holder of ADSs or Class A ordinary shares in any year in which we are a PFIC will be required to file Internal Revenue Service Form 8621 regarding distributions received on the ADSs or Class A ordinary shares and any gain realized on the disposition of the ADSs or Class A ordinary shares. In addition, if we are a PFIC for a taxable year in which we pay a dividend, or for the prior taxable year, the lower rate on “qualified dividend income” discussed above with respect to dividends paid to certain non-corporate U.S. holders would not apply.

U.S. holders and prospective holders of our ADSs are urged to consult their tax advisors regarding the application of the PFIC rules to an investment in ADSs or Class A ordinary shares.

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

Dividend payments with respect to ADSs or Class A ordinary shares and proceeds from the sale, exchange or redemption of ADSs or Class A ordinary shares may be subject to information reporting to the Internal Revenue Service and possible United States backup withholding at a current rate of 28%. Backup withholding will not apply, however, to a U.S. holder who furnishes a correct taxpayer identification number and makes any other required certification or who is otherwise exempt from backup withholding. U.S. holders who are required to establish their exempt status must provide such certification on Internal Revenue Service Form W-9. U.S. holders should consult their tax advisors regarding the application of the United States information reporting and backup withholding rules.

Individual U.S. holders, and certain entities that are U.S. holders, that own “specified foreign financial assets” with an aggregate value in excess of \$50,000 are generally required to file an information statement along with their tax returns, currently on Form 8938, with respect to such assets. “Specified foreign financial assets” include any financial accounts held at a non-U.S. financial institution, as well as securities issued by a non-U.S. issuer (which would include our ADSs and Class A ordinary shares) that are not held in accounts maintained by financial institutions. Higher reporting thresholds apply to certain individuals living abroad and to certain married individuals. Regulations have been proposed that would extend this reporting requirement to certain entities that are treated as formed or availed of to hold direct or indirect interests in specified foreign financial assets based on certain objective criteria. U.S. holders who fail to report the required information could be subject to substantial penalties. Prospective investors should consult their own tax advisors concerning the application of these rules to their investment in our ADSs, including the application of the rules to their particular circumstances.

### ***Available Additional Information***

We are subject to the periodic reporting and other informational requirements of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Under the Exchange Act, we are required to file reports and other information with the SEC.

Copies of reports and other information, when so filed, may be inspected without charge and may be obtained at prescribed rates at the public reference facilities maintained by the Securities and Exchange Commission at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. The public may obtain information regarding the Washington, D.C. Public Reference Room by calling the Commission at 1-800-SEC-0330. The SEC also maintains a Website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding registrants that make electronic filings with the SEC using its EDGAR system. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of quarterly reports and proxy statements, and officers, directors and principal shareholders are exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act.

As permitted under NASDAQ Stock Market Rule 5250(d)(1)(C), we will post our annual reports filed with the SEC on our Web site at <http://www.changyou.com>. We will not furnish hard copies of such reports to holders of our ADSs unless we are requested to do so in writing by a holder. Upon receipt of such a request, we will provide a hard copy of such reports to such requesting holder free of charge.

**ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.*****Foreign Currency Exchange Risk***

While our reporting currency is the U.S. dollar, to date the majority of our revenues and costs are denominated in RMB and a significant portion of our assets and liabilities are denominated in RMB. As a result, we are exposed to foreign exchange risk as our revenues and results of operations may be affected by fluctuations in the exchange rate between U.S. dollar and RMB. If the RMB depreciates against the U.S. dollar, the value of our RMB revenues and assets as expressed in our U.S. dollar financial statements will decline. For example, as reported in our U.S. dollar financial statements included in this annual report, our revenues for the year ended December 31, 2013 were \$737.9 million and our total assets as of December 31, 2013 were \$1.6 billion, representing revenues of RMB 4.6 billion and total assets of RMB 9.7 billion at the noon buying rate of RMB 6.0969 to \$1.00 on December 31, 2013. If the value of the RMB were to depreciate by approximately 10% to RMB 6.7066 to \$1.00, the value of the same amount of RMB-denominated revenue and total assets in U.S. dollars would be \$670.8 million and \$1.4 billion, respectively. We do not hold any derivative or other financial instruments that expose us to substantial market risk. See “Risk Factors—Risks Related to Doing Business in China—Fluctuation in the value of the RMB may have an adverse effect on our shareholders’ investment.” in Item 3.

The RMB is currently freely convertible under the “current account,” which includes dividends, trade and service-related foreign exchange transactions, but not under the “capital account,” which includes foreign direct investment. In addition, commencing on July 21, 2005, China reformed its exchange rate regime by changing to a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies. Provisions on Administration of Foreign Exchange, as amended in August 2008, further changed China’s exchange regime to a managed floating exchange rate regime based on market supply and demand. Under the managed floating exchange rate regime, the RMB is no longer pegged to the U.S. dollar. The exchange rate of the RMB against the U.S. dollar was adjusted to RMB 8.11 per U.S. dollar as of July 22, 2005, representing an appreciation of about 2%. The People’s Bank of China will announce the closing prices of foreign currencies such as the U.S. dollar traded against the RMB in the inter-bank foreign exchange market after the closing of the market on each business day, and will make such prices the central parity for trading against the RMB on the following business day. On May 19, 2007, the People’s Bank of China announced a policy to expand the maximum daily floating range of RMB trading prices against the U.S. dollar in the inter-bank spot foreign exchange market from 0.3% to 0.5%. While the international reactions to the RMB revaluation and widening of the RMB’s daily trading band have generally been positive, with the increased floating range of the RMB’s value against foreign currencies, the RMB may appreciate or depreciate significantly in value against the U.S. dollar or other foreign currencies in the long term, depending on the fluctuation of the basket of currencies against which it is currently valued. To date, we have not entered into any hedging transactions in an effort to reduce our exposure to foreign currency exchange risk. While we may decide to enter into hedging transactions in the future, the effectiveness of these hedges may be limited and we may not be able to successfully hedge our exposure. Accordingly, we may incur economic losses in the future due to foreign exchange rate fluctuations, which could have a negative impact on our financial condition and results of operations.

The following table sets forth a summary of our foreign currency sensitive financial instruments as of December 31, 2013, which consisted of cash and cash equivalents, restricted time deposits, accounts receivable, short term investments, prepaid and other current assets, short-term bank loans, other current liabilities, long-term accounts payables, long-term bank loans and long-term contingent consideration. The book value of those financial instruments approximated their fair value.

	US\$	Denominated in		Total
		RMB	Others	
		(in thousands)		
Cash and cash equivalents	\$ 99,292	\$440,697	\$8,495	\$548,484
Restricted time deposits	—	424,674	—	424,674
Accounts receivable, net	1,359	34,280	357	35,996
Short-term investments	—	2,827	—	2,827
Prepaid and other current assets	722	63,103	632	64,457
Short-term bank loans	307,000	103,331	—	410,331
Other current liabilities	4,770	227,234	6,613	238,617
Long-term accounts payable	—	6,252	—	6,252

***Inflation Rate Risk***

According to the National Bureau of Statistics of China, the change in the consumer price index in China was 2.6%, 2.6% and 5.4% in 2013, 2012 and 2011, respectively. If inflation rises, it may materially and adversely affect our business.

***Interest Rate Risk***

Our investment policy limits our investments of excess cash in high-quality corporate securities and limits the amount of credit exposure to any one issuer. We protect and preserve our invested funds by limiting default, market and reinvestment risk.



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During 2013, we drew down loans from the offshore branches of certain banks, which were secured by an equivalent or greater amount of RMB deposits by us in the onshore branches of such banks. As of December 31, 2013, the total amount of the loans was \$410.3 million, of which \$307.0 million carried a floating rate of interest based on the London Inter-Bank Offered Rate, or LIBOR, and \$103.3 million carried a fixed rate of interest. The fair value of our fixed interest rate loans will fluctuate with movements of market interest rates, increasing in periods of declining rates of interest and declining in periods of increasing rates of interest. Based upon the prevailing interest rates in the market, the fair value of our loans was \$410.3 million at December 31, 2013.





**ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

The following table summarizes the fees and charges that a holder of our ADSs may have to pay, directly or indirectly, pursuant to the Deposit Agreement, which was filed as an exhibit to our Registration Statement on Form F-1 filed with the SEC on March 17, 2009 (File No. 333-158061), and the types of services and the amount of the fees or charges paid therefore:

<i>Persons depositing or withdrawing shares or ADS holders must pay:</i>	<i>For:</i>
\$5.00 (or less) per 100 ADSs (or portion of 100 ADSs)	<ul style="list-style-type: none"> <li>• Issuance of ADSs, including issuances resulting from a distribution of shares or rights or other property</li> </ul>
\$0.02 (or less) per ADS	<ul style="list-style-type: none"> <li>• Cancellation of ADSs for the purpose of withdrawal, including if the Deposit Agreement terminates</li> <li>• Any cash distribution to ADS holders</li> </ul>
A fee equivalent to the fee that would be payable if securities distributed to you had been shares and the shares had been deposited for issuance of ADSs	<ul style="list-style-type: none"> <li>• Distribution of securities distributed to holders of deposited securities which are distributed by the depositary to ADS holders</li> </ul>
\$0.02 (or less) per ADSs per calendar year	<ul style="list-style-type: none"> <li>• Depositary services</li> </ul>
Registration or transfer fees	<ul style="list-style-type: none"> <li>• Transfer and registration of shares on our share register to or from the name of the depositary or its agent when you deposit or withdraw shares</li> </ul>
Expenses of the depositary	<ul style="list-style-type: none"> <li>• Cable, telex and facsimile transmissions (when expressly provided in the Deposit Agreement)</li> <li>• converting foreign currency to U.S. dollars</li> </ul>
Taxes and other governmental charges the depositary or the custodian have to pay on any ADS or share underlying an ADS, for example, stock transfer taxes, stamp duty or withholding taxes	<ul style="list-style-type: none"> <li>• As necessary</li> </ul>
Any charges incurred by the depositary or its agents for servicing the deposited securities	<ul style="list-style-type: none"> <li>• As necessary</li> </ul>

Pursuant to an agreement dated April 1, 2009, as amended in June 4, 2010, between us and the Bank of New York Mellon, the depositary for our ADSs, the depositary reimbursed us in May of each of 2009, 2010, 2011, 2012 and 2013 for our expenses, including investor relations expenses, legal fees, accounting fees, NASDAQ listing application and listing fees and related expenses, of \$1,087,000, \$6,000, \$9,000, \$6,000 and \$6,000, respectively, which is net of U.S. withholding tax, related to the establishment of an American depositary receipt facility.



## PART II

### ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

Not Applicable.

### ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

#### *Use of Proceeds*

On April 1, 2009, our registration statement on Form F-1 (File No. 333-158061), as amended, was declared effective by the SEC for our initial public offering, pursuant to which we and Sohu.com (Game) Limited, an indirect wholly-owned subsidiary of Sohu and the selling shareholder in the offering, offered and sold a total of 8,625,000 ADSs at the public offering price of \$16.00 per ADS. The offering was completed on April 7, 2009.

We sold 3,750,000 ADSs and the selling shareholder sold 4,875,000 ADSs in our initial public offering. We received net proceeds of approximately \$54.7 million, after deducting underwriting discounts and commissions of approximately \$4.2 million and other expenses of approximately \$1.1 million. None of the underwriting discounts and commissions or other expenses were paid directly or indirectly to any director, officer, or general partner of ours or to their associates, persons owning ten percent or more of any class of our equity securities, or to any of our affiliates. We did not receive any proceeds from the sale of our ADSs by the selling shareholder. Credit Suisse Securities (USA) LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated were the managing underwriters for the offering.

As of December 31, 2013, we had not used any of the net proceeds to us from our initial public offering. Proceeds from the offering have been deposited in banks.

### ITEM 15. CONTROLS AND PROCEDURES

#### *Disclosure Controls and Procedures*

As of the end of the period covered by this annual report, our principal executive officer and principal financial officer have performed an evaluation of the effectiveness of our disclosure controls and procedures as defined and required under Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Based upon that evaluation, they have concluded that our disclosure controls and procedures were effective in ensuring that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure. Our principal executive officer and principal financial officer also concluded that the information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in by the Securities and Exchange Commission's rules and regulations.

#### *Management's Annual Report on Internal Control over Financial Reporting*

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with U.S. GAAP. Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of are being made only in accordance with authorizations of management; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of any of our assets that could have a material effect on the financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an assessment of the effectiveness of our internal control over financial reporting based upon criteria established in the "Internal Control—Integrated Framework (1992)" issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on this assessment, management has concluded that our internal control over financial reporting is effective as of December 31, 2013.

The effectiveness of our internal control over financial reporting as of December 31, 2013 has been audited by PricewaterhouseCoopers Zhong Tian LLP, our independent registered public accounting firm, as stated in its report included on page F-2.



***Changes in Internal Control over Financial Reporting***

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15 or 15d-15 that occurred during the period covered by this annual report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.



#### ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Our Board of Directors has determined that Dave De Yang is an “audit committee financial expert” as defined under the applicable SEC rules and Rule 5605(c)(2) of the NASDAQ Listing Rules. Our Board of Directors has determined that all three members of our audit committee are “independent” under Rule 10A-3 under the Securities Exchange Act of 1934 and Rule 5605 of the NASDAQ Listing Rules.

#### ITEM 16B. CODE OF ETHICS

Our Board of Directors adopted a code of ethics and conduct that is applicable to all of our directors, officers and employees. A copy of our code of ethics and conduct was filed as an exhibit to our Registration Statement on Form F-1 (File No. 333-158061) originally filed with the SEC on March 17, 2009, and is also posted on our Website at <http://www.changyou.com> under the “Investor Relations—Corporate Governance.”

#### ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The following table sets forth the aggregate fees by categories specified below in connection with certain professional services rendered by PricewaterhouseCoopers Zhong Tian LLP, our principal external auditors, for the periods indicated below.

	For the year ended December 31,	
	2012	2013
	US\$	US\$
	(in thousands)	
Audit fees <sup>(1)</sup>	\$1,562	\$1,977
Audit related fees <sup>(2)</sup>	719	65
Tax fees <sup>(3)</sup>	630	835
All other fees	2	131
<b>Total</b>	<b>\$2,913</b>	<b>\$3,008</b>

- (1) “Audit fees” means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal auditors for the audit of our annual financial statements and our internal controls over financial reporting.
- (2) “Audit-related fees” means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal auditors related to the audit of our financial statements and our internal controls over financial reporting that are not reported under “Audit Fees” and consultation on accounting standards or transactions.
- (3) “Tax fees” means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal auditors for tax compliance and tax advice.

#### *Audit Committee Pre-approval Policies and Procedures*

Our audit committee has adopted procedures which set forth the manner in which the committee will review and approve all audit and non-audit services to be provided by PricewaterhouseCoopers Zhong Tian LLP before that firm is retained for such services. The pre-approval procedures are as follows:

- Any audit or non-audit service to be provided to us by the independent accountant must be submitted to the audit committee for review and approval, with a description of the services to be performed and the fees to be charged.
- The audit committee in its sole discretion then approves or disapproves the proposed services and documents such approval, if given, through written resolutions or in the minutes of meetings, as the case may be.

**ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

Not Applicable.

**ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

On July 29, 2013, we announced that our board of directors had authorized a share repurchase program of up to US\$100 million of our outstanding American depositary shares, or ADSs, over a two-year period from July 27, 2013 to July 26, 2015. The ADSs may be purchased from time to time at management's discretion at prevailing market prices in the open market in accordance with Rule 10b-18 under the Securities Exchange Act of 1934. Changyou's management will determine the timing and amount of any purchases of Changyou ADSs based on their evaluation of market conditions, the trading price of our ADSs and other factors. The purchase program may be suspended or discontinued at any time. As of December 31, 2013, we had repurchased an aggregate of 590,500 ADSs, representing 1,181,000 Class A ordinary shares, for an aggregate purchase price of \$17.25 million (equivalent to an average price of \$29.2 per ADS, or \$14.6 per Class A ordinary share). All ADSs repurchased by us during 2013 were made pursuant to our publicly announced share repurchase program. We financed the share repurchase program through U.S. dollar-denominated loans from offshore banks which are secured by an equivalent amount of RMB-denominated onshore bank deposits of our subsidiaries in China.

The table below provides additional information on our repurchases of ADSs for each month of 2013 after the commencement of the program:

2013 Month	Number of ADSs Purchased	Purchase Price (US\$)*	Average Price Paid Per ADS (US\$)*	Average Price Paid Per Ordinary Share (US\$)*
August (from August 9 to August 21)	227,500	6,796,182	29.87	14.94
September (from September 3 to September 6)	78,300	2,258,222	28.84	14.42
October (from October 28 to October 30)	284,700	8,197,604	28.79	14.40
<b>Total</b>	<b>590,500</b>	<b>17,252,008</b>	<b>29.22</b>	<b>14.61</b>

\* Cost and average price data includes trading commissions. Some numbers may not add due to rounding.

**ITEM 16F. CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT**

Not Applicable.

**ITEM 16G. CORPORATE GOVERNANCE**

Because Sohu owns more than 50% of the total voting power of our ordinary shares, we are a "controlled company" under the NASDAQ Listing Rules. We intend to rely on certain exemptions that are available to controlled companies from NASDAQ corporate governance requirements, including the requirements:

- that we have a corporate governance and nominating committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities;
- that we have a compensation committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities; and
- for an annual performance evaluation of the nominating and governance committee and compensation committee.

We are not required to and will not voluntarily meet these requirements. As a result of our use of the "controlled company" exemptions, our investors will not have the same protection afforded to shareholders of companies that are subject to all of NASDAQ's corporate governance requirements.

**ITEM 16H. MINE SAFETY DISCLOSURE**

Not Applicable.





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**PART III**

**ITEM 17. FINANCIAL STATEMENTS**

We have elected to provide financial statements pursuant to Item 18.

**ITEM 18. FINANCIAL STATEMENTS**

The consolidated financial statements of Changyou and its subsidiaries and VIEs are included at the end of this annual report.



## ITEM 19. EXHIBITS

<u>Exhibit Number</u>	<u>Description of Document</u>
1.1	Second Amended and Restated Memorandum and Articles of Association of the Registrant (incorporated by reference to Exhibit 3.1 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
2.1	Registrant's Specimen American Depositary Receipt (incorporated by reference to Exhibit 4.1 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
2.2	Registrant's Specimen Certificate for Class A ordinary shares (incorporated by reference to Exhibit 4.2 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
2.3	Form of Deposit Agreement among the Registrant, the depositary and all registered holders and beneficial owners of the American Depositary Shares (incorporated by reference to Exhibit 4.3 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.1	2008 Share Incentive Plan (incorporated by reference to Exhibit 10.1 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.2	Form of Indemnification Agreement with the Registrant's directors (incorporated by reference to Exhibit 10.2 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.3	Form of Executive Employment Agreement with Executive Officers (incorporated by reference to Exhibit 10.3 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.4	Form of Executive Employee Non-Competition, Non-Solicitation Agreement, Confidential Information and Work Product Agreement with Executive Officers (incorporated by reference to Exhibit 10.4 to our Registration Statement on Form F-1 (file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.5	Share Subscription Agreement between Registrant and Prominence Investments Limited (incorporated by reference to Exhibit 10.5 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.6	Form of Restricted Share Unit Agreement with Executive Officers (incorporated by reference to Exhibit 10.6 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.7	Form of Restricted Share Unit Agreement between Registrant and certain executive officers and employees (incorporated by reference to Exhibit 10.7 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.8	English translation of Form of Loan Agreements, dated August 20, 2008, between Beijing AmazGame Age Internet Technology Co., Ltd (or AmazGame) and Tao Wang and between AmazGame and a Changyou employee (incorporated by reference to Exhibit 10.8 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.9	English translation of Form of Equity Interest Purchase Right Agreements, dated August 20, 2008, between AmazGame and Tao Wang and between AmazGame and a Changyou employee (incorporated by reference to Exhibit 10.9 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.10	English translation of Form of Equity Pledge Agreements, dated August 20, 2008, between AmazGame and Tao Wang and between AmazGame and a Changyou employee (incorporated by reference to Exhibit 10.10 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.11	English translation of Form of Powers of Attorney, dated August 20, 2008, by Tao Wang in favor of AmazGame and by a Changyou employee in favor of AmazGame (incorporated by reference to Exhibit 10.11 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)



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**CHANGYOU.COM LIMITED**

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<u>Exhibit Number</u>	<u>Description of Document</u>
4.12	English translation of Business Operation Agreement, dated August 20, 2008, between AmazGame and Gamease, Tao Wang and a Changyou employee (incorporated by reference to Exhibit 10.12 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.13	English translation of Services and Maintenance Agreement, dated November 30, 2007, between AmazGame and Gamease (incorporated by reference to Exhibit 10.13 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.14	English translation of Technology Support and Utilization Agreement, dated August 20, 2008, between AmazGame and Gamease (incorporated by reference to Exhibit 10.14 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.15	Master Transaction Agreement, dated January 1, 2009, by and between Sohu.com Inc. and Changyou.com Limited (or Changyou) (incorporated by reference to Exhibit 10.15 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.16	Non-Competition Agreement, dated January 1, 2009, between Sohu.com Inc. and Changyou (incorporated by reference to Exhibit 10.16 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.17	Marketing Services Agreement, dated January 1, 2009, between Sohu.com Inc. and Changyou (incorporated by reference to Exhibit 10.17 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.18	English translation of Asset Transfer Agreement, dated November 23, 2007, between Beijing Sohu New Era Information Technology Co., Ltd. (or Sohu Era) and AmazGame (incorporated by reference to Exhibit 10.18 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.19	English translation of Asset Transfer Agreement, dated November 23, 2007, between Sohu Era and Gamease (incorporated by reference to Exhibit 10.19 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.20	English translation of Service Transfer Agreement, effective as of December 1, 2007, between Sohu Era and Gamease (incorporated by reference to Exhibit 10.20 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.21	English translation of Technology Transfer Agreement, dated November 10, 2007, between Beijing Fire Fox Digital Technology Co. Ltd. (or Beijing Fire Fox) and Gamease (incorporated by reference to Exhibit 10.21 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.22	English translation of Trademark Assignment Agreement, dated November 28, 2007, between Beijing Fire Fox and Gamease (incorporated by reference to Exhibit 10.22 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.23	TLBB License Agreement, dated March 30, 2007, among Beijing Sohu Internet Information Service Co., Ltd. (or Sohu Internet), Beijing Fire Fox and FPT Telecom (incorporated by reference to Exhibit 10.23 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)†
4.23.1	Supplement to Game License Agreement, dated December 1, 2007, among Sohu Internet, Beijing Fire Fox, Gamease and FPT Telecom (incorporated by reference to Exhibit 10.23.1 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.24	English translation of Operation Agreement effective as of August 23, 2007 between Gamease and Beijing Pixel Software Technology Co. Ltd. (incorporated by reference to Exhibit 10.24 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.25	English translation of Trademark License Agreement, effective as of August 23, 2007, between Gamease and Beijing Pixel Software Technology Co. Ltd. (incorporated by reference to Exhibit 10.25 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)



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<u>Exhibit Number</u>	<u>Description of Document</u>
4.26	English Translation of LAW Game Software License Agreement, dated December 3, 2007, between Gamease and Guangzhou No. 9 Art Network Technology Co. Ltd. (incorporated by reference to Exhibit 10.26 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)†
4.27	English Translation of TLBB License Agreement (Taiwan), dated December 25, 2007, between Gamease and (Taiwan) Zhi Guan Technology Co. Ltd. (incorporated by reference to Exhibit 10.27 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)†
4.28	English Translation of TLBB License Agreement (Hong Kong and Macau), dated December 5, 2007, between Gamease and Zhi Ao Online Games Group Co. Ltd. (incorporated by reference to Exhibit 10.28 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009) †
4.29	English Translation of License Agreement regarding Immortal Faith, dated July 21, 2008, between Gamease and Beijing Game Top Software Co. Limited (incorporated by reference to Exhibit 10.29 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009) †
4.30	English Translation of License Agreement between Gamease and Louis Cha regarding TLBB (incorporated by reference to Exhibit 10.30 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)†
4.31	English Translation of License Agreement between Gamease and Louis Cha regarding DMD (incorporated by reference to Exhibit 10.31 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)†
4.32	English Translation of License Agreement between Gamease and Louis Cha regarding TLBB (incorporated by reference to Exhibit 10.32 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009) †
4.33	English Translation of Premises Lease Agreement, dated October 16, 2007, between AmazGame and Beijing Jing Yan Hotel Co. Ltd. (incorporated by reference to Exhibit 10.33 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
4.34	English Translation of Zhong Hua Ying Xiong License Agreement, dated September 30, 2009, between AmazGame and Dragon Online (Beijing) Technology Co., Ltd. † (incorporated by reference to Exhibit 4.34 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 26, 2010) †
4.35	English Translation of Real Estate Purchase Agreement, dated August 8, 2009, between AmazGame and Beijing Yinhe Wanda Real Estate Co., Ltd. (incorporated by reference to Exhibit 4.35 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 26, 2010)
4.36	English Translation of Project Cooperation Agreement, dated August 23, 2010, between AmazGame and Beijing Raycom Jingyuan Real Estate Development Co., Ltd. (incorporated by reference to Exhibit 4.36 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.37	Amended and Restated Marketing Services Agreement, dated January 1, 2010, between Changyou and Sohu(incorporated by reference to Exhibit 4.37 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.38	English translation of Form of Loan Agreements, dated September 1, 2010, between Beijing Changyou Gamespace Software Technology Co., Ltd (or Gamespace) and Tao Wang and between Gamespace and Dewen Chen(incorporated by reference to Exhibit 4.38 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.39	English translation of Form of Equity Interest Purchase Right Agreements, dated September 1, 2010, among Gamespace, Beijing Guanyou Gamespace Digital Technology Co., Ltd. (or Guanyou Gamespace) and Tao Wang and among Gamespace, Guanyou Gamespace and Dewen Chen(incorporated by reference to Exhibit 4.39 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)



<u>Exhibit Number</u>	<u>Description of Document</u>
4.40	English translation of Form of Equity Pledge Agreements, dated September 1, 2010, among Gamespace, Guanyou Gamespace and Tao Wang and among Gamespace, Guanyou Gamespace and Dewen Chen (incorporated by reference to Exhibit 4.40 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.41	English translation of Form of Powers of Attorney, dated September 1, 2010, by Tao Wang in favor of Gamespace and by Dewen Chen in favor of Gamespace (incorporated by reference to Exhibit 4.41 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.42	English translation of Business Operation Agreement, dated September 1, 2011, between Gamespace and Guanyou Gamespace, Tao Wang and Dewen Chen (incorporated by reference to Exhibit 4.42 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.43	English translation of Services and Maintenance Agreement, dated September 1, 2010, between Gamespace and Guanyou Gamespace (incorporated by reference to Exhibit 4.43 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.44	English translation of Technology Support and Utilization Agreement, dated September 1, 2010, between Gamespace and Guanyou Gamespace (incorporated by reference to Exhibit 4.44 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.45	English translation of Exclusive Business Cooperation Agreement, dated September 11, 2007, between ICE Information Technology (Shanghai) Co., Ltd (or ICE Information) and Shanghai ICE Information Technology Co., Ltd.(or Shanghai ICE) (incorporated by reference to Exhibit 4.45 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.46	English translation of Exclusive Technology Consulting and Service Agreement, dated September 11, 2007, between ICE Information and Shanghai ICE (incorporated by reference to Exhibit 4.46 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.47	English translation of Business Operation Agreement, among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE (incorporated by reference to Exhibit 4.47 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.48	English translation of Call Option Agreement, among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE (incorporated by reference to Exhibit 4.48 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.49	English translation of Form of Share Pledge Agreement, among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE(incorporated by reference to Exhibit 4.49 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2011)
4.50	English translation of Share Transfer Framework Agreement, between, on the one hand, Gamease and Changyou, and, on the other hand, 7Road and its shareholders, relating to the transfer of 68.258% equity interests in each of 7Road and its overseas affiliate, dated April 22, 2011(incorporated by reference to Exhibit 4.50 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.51	Master Transaction Agreement, dated as of November 29, 2011, between, on the one hand, Sohu.com Inc., Sohu.com Limited, Beijing Sohu Internet Information Service Co., Ltd., Beijing Sohu New Era Information Technology Co., Ltd., and Beijing Sohu New Media Information Technology Co., Ltd., and, on the other hand, Changyou.com Limited, Changyou.com HK Limited, and Beijing Changyou Gamespace Software Technology Co., Ltd., Beijing Guanyou Gamespace Digital Technology Co., Ltd. (incorporated by reference to Exhibit 4.51 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.52	Amended and Restated Non-Competition Agreement, dated as of November 29, 2011, by and between Sohu.com Inc. and Changyou.com Limited (incorporated by reference to Exhibit 4.52 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.53	Services Agreement, dated as of November 29, 2011, by and between Beijing Changyou Gamespace Software Technology Co., Ltd. and Beijing Sohu New Media Information Technology Co., Ltd. (incorporated by reference to Exhibit 4.53 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)





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<u>Exhibit Number</u>	<u>Description of Document</u>
4.54	Online Links and Advertising Agreement, dated as of November 29, 2011, by and between Beijing Guanyou Gamespace Digital Technology Co., Ltd. and Beijing Sohu New Media Information Technology Co., Ltd. (incorporated by reference to Exhibit 4.54 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.55	Form of Executive Employment Agreement dated as of January 1, 2012 with Executive Officers (incorporated by reference to Exhibit 4.55 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.56	Form of Executive Employee Non-Competition, Non-Solicitation Agreement, Confidential Information and Work Product Agreement dated January 1, 2012 with Executive Officers (incorporated by reference to Exhibit 4.56 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.57	English Translation of Form of Beijing Commercial Property Advance Sale Contract between AmazGame and Beijing Raycom Jingyuan Real Estate Development Co., Ltd. (incorporated by reference to Exhibit 4.57 to our Annual Report on Form 20-F filed with the Securities and Exchange Commission on February 28, 2012)
4.58	English Translation of Loan Assignment and Equity Interest Transfer Agreement, dated June 23, 2010, between AmazGame, Gamease, Yaobin Wang, Dewen Chen and Tao Wang
4.59	English translation of Loan Agreement, dated June 23, 2010, between AmazGame and Dewen Chen
4.60	English translation of Equity Interest Purchase Right Agreement, dated June 23, 2010, among AmazGame, Gamease and Dewen Chen
4.61	English translation of Equity Interest Pledge Agreement, dated June 23, 2010, between AmazGame, Gamease and Dewen Chen
4.62	English translation of Form of Powers of Attorney, dated June 23, 2010, by Tao Wang in favor of AmazGame and by Dewen Chen in favor of AmazGame
4.63	English translation of Business Operation Agreement, dated June 23, 2010, between AmazGame and Gamease, Tao Wang and Dewen Chen
4.64	7Road.com Limited 2012 Share Incentive Plan, as amended and restated on November 2, 2012
4.65	Form of Equity Interest Purchase Right Agreements, dated June 26, 2012, among 7Road Technology, Shenzhen 7Road and each of the shareholders of Shenzhen 7Road (English Translation)
4.66	Form of Equity Interest Pledge Agreements, dated June 26, 2012, among 7Road Technology, Shenzhen 7Road and each of the shareholders of Shenzhen 7Road (English Translation)
4.67	Form of Power of Attorney, dated June 26, 2012, by each of the shareholders of Shenzhen 7Road in favor of 7Road Technology (English Translation)
4.68	Form of Spousal Consent, dated June 26, 2012, by the spouse of each of the shareholders of Shenzhen 7Road who is a married individual (English Translation)
4.69	Business Operation Agreement, dated June 26, 2012, among 7Road Technology, Shenzhen 7Road, Beijing Gamease Age Digital Technology Co., Ltd and four individual shareholders of Shenzhen 7Road (English Translation)†
4.70	Technology Development and Utilization Service Agreement, dated June 26, 2012, between 7Road Technology and Shenzhen 7Road (English Translation)
4.71	Services and Maintenance Agreement, dated June 26, 2012, between 7Road Technology and Shenzhen 7Road (English Translation)
4.72	Loan Facility Letter, dated July 4, 2012, between Hang Seng Bank Limited and Changyou.com HK Limited
4.73	Loan Facility Letter, dated July 12, 2012, between the Bank of East Asia, Limited and Changyou.com HK Limited
4.74	Loan Facility Letter, dated August 7, 2012, between the Bank of Communications Co., Ltd. Hong Kong Branch and Changyou.com HK Limited



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<u>Exhibit Number</u>	<u>Description of Document</u>
4.75	Loan Facility Letter amendment, dated August 3, 2012, between Hang Seng Bank Limited and Changyou.com HK Limited
4.76	Executive Employment Agreement with Wendy Pan, dated as of February 20, 2013
4.77	Executive Employee Non-Competition, Non-Solicitation Agreement, Confidential Information and Work Product Agreement with Wendy Pan, dated as of February 20, 2013
4.78*	Acquisition Framework Agreement, between Changyou, 7Road and its shareholders, relating to the transfer of 31.742% equity interests in Shenzhen 7Road and all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders, representing 28.074% of the outstanding share capital of 7Road Cayman, dated May 1, 2013 (English translation) †
4.79*	Amended and Restated Equity Interest Purchase Right Agreement, dated June 5, 2013, among 7Road Technology, Shenzhen 7Road and Gamease (English Translation)
4.80*	Amended and Restated Equity Interest Pledge Agreement, dated June 5, 2013, among 7Road Technology, Shenzhen 7Road and Gamease (English Translation)
4.81*	Power of Attorney, dated June 5, 2013, by Gamease in favor of 7Road Technology (English Translation)
4.82*	Amended and Restated Business Operation Agreement, dated June 5, 2013, among 7Road Technology, Shenzhen 7Road and Gamease (English Translation)
4.83*	Supplemental Agreement (to the Technology Development and Utilization Service Agreement) dated June 5, 2013, between 7Road Technology and Shenzhen 7Road (English Translation)
4.84*	Supplemental Agreement ( to the Services and Maintenance Agreement) dated June 5, 2013, between 7Road Technology and Shenzhen 7Road (English Translation)
4.85*	Loan Facility Letter, dated August 13, 2013, among Hang Seng Bank Limited, Changyou.com HK Limited and Changyou.com Limited
4.86*	Loan Facility Letter, dated July 26, 2013, between the Bank of East Asia, Limited and Changyou.com Limited
4.87*	Loan Facility Letter, dated May 8, 2013, among Hang Seng Bank Limited , Changyou.com HK Limited and Changyou.com Limited
4.88*	Investment Agreement, dated November 19, 2013, among Koram Games Limited, Heroic Vision Holdings Limited, Beijing Kunlun Tech Co., Ltd., Guangzhou Kunlun Online Information Tech Co., Ltd. and Kunlun Korea Co., Ltd (English Translation) †
4.89*	Supplementary Agreement to Investment Agreement, dated December 24, 2013, among Koram Games Limited, Heroic Vision Holdings Limited, Beijing Kunlun Tech Co., Ltd., Guangzhou Kunlun Online Information Tech Co., Ltd. and Kunlun Korea Co., Ltd (English Translation) †
4.90*	Shareholder Agreement, dated November 19, 2013, between Koram Games Limited, Heroic Vision Holdings Limited and TalkTalk Limited (English Translation) †
8.1*	Subsidiaries of the Registrant
11.1	Code of Ethics and Conduct for Directors, Officers and Employees (incorporated by reference to Exhibit 99.1 to our Registration Statement on Form F-1(file no. 333-158061) filed with the Securities and Exchange Commission on March 17, 2009)
12.1*	Certification of Chief Executive Officer Required by Rule 13a-14(a)
12.2*	Certification of Chief Financial Officer Required by Rule 13a-14(a)
13.1*	Certification of Chief Executive Officer Required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code
13.2*	Certification of Chief Financial Officer Required by Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code
15.1*	Consent of PricewaterhouseCoopers Zhong Tian LLP, an independent registered public accounting firm
15.2*	Consent of Haiwen & Partners



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<u>Exhibit Number</u>	<u>Description of Document</u>
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document

† Portions of these exhibits have been omitted pursuant to a request for confidential treatment, and the omitted information has been filed separately with the Securities and Exchange Commission.

\* Filed or furnished with this Annual Report on Form 20-F.



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**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing its annual report on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

CHANGYOU.COM LIMITED

By /s/ TAO WANG  
Name: **Tao Wang**  
Title: **Chief Executive Officer**

By /s/ ALEX HO  
Name: **Alex Ho**  
Title: **Chief Financial Officer**

Date: February 28, 2014



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<u>Consolidated Balance Sheets as of December 31, 2012 and 2013</u>	F-3
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**Report of Independent Registered Public Accounting Firm**

To Board of Directors and Shareholders of Changyou.com Limited:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of comprehensive income, consolidated statements of shareholders' equity and consolidated statements of cash flows present fairly, in all material respects, the financial position of Changyou.com Limited (the "Company") and its subsidiaries at December 31, 2013 and December 31, 2012, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control—Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in management's annual report on internal control over financial reporting appearing under Item 15 of the accompanying Form 20-F. Our responsibility is to express opinions on these financial statements and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PricewaterhouseCoopers Zhong Tian LLP  
Beijing, the People's Republic of China  
February 28, 2014

## CHANGYOU.COM LIMITED

## CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2012 and 2013

(In thousands, except par value)

	Notes	As of December 31,	
		2012	2013
		US\$	US\$
<b>Assets</b>			
<b>Current assets:</b>			
Cash and cash equivalents		366,639	548,484
Short-term investments	4(g)	51,720	2,827
Accounts receivable, net	8	23,364	35,996
Prepaid and other current assets (including \$10,101 and \$10,104, respectively, of short-term prepayment to a related party)	9	29,045	64,457
Due from Sohu	26	495	393
Restricted time deposits	4(e), 7	116,140	393,019
<b>Total current assets</b>		<b>587,403</b>	<b>1,045,176</b>
<b>Non-current assets:</b>			
Fixed assets, net	10	64,828	246,674
Intangible assets, net	11	54,249	73,395
Equity investments	12	850	—
Goodwill	13	134,921	180,252
Restricted time deposits	4(e), 7	130,459	31,655
Other assets, net (including \$10,138 and \$259, respectively, of long-term prepayment to a related party)	14	141,803	8,060
<b>Total assets</b>		<b>1,114,513</b>	<b>1,585,212</b>
<b>Liabilities, mezzanine equity and shareholders' equity</b>			
<b>Current liabilities:</b>			
Accounts payable (including \$2,223 and \$332, respectively, of accounts payable to a related party and accounts payable of consolidated variable interest entities ("VIEs") without recourse to the Company of \$8,677 and \$25,986, respectively)		32,750	57,438
Receipts in advance and deferred revenue (including receipts in advance and deferred revenue of consolidated VIEs without recourse to the Company of \$43,027 and \$43,252, respectively)	16	43,659	43,842
Accrued salary and benefits (including accrued salary and benefits of consolidated VIEs without recourse to the Company of \$3,474 and \$2,316, respectively)		33,824	49,450
Accrued liabilities to suppliers (including accrued liabilities to suppliers of consolidated VIEs without recourse to the Company of \$6,555 and \$9,314, respectively)		12,863	22,987
Tax payables (including tax payables of consolidated VIEs without recourse to the Company of \$9,923 and \$1,453, respectively)		17,825	31,214
Short-term bank loans	4(e), 7	113,000	410,331
Other accrued liabilities (including other accrued liabilities of consolidated VIEs without recourse to the Company of \$28,004 and \$9,530, respectively)	17	32,159	14,872
Deferred tax liabilities		11,878	18,814
<b>Total current liabilities</b>		<b>297,958</b>	<b>648,948</b>
<b>Long-term liabilities:</b>			
Long-term accounts payable (including \$2,290 and \$nil, respectively, of long-term accounts payable to a related party)		12,683	6,252
Long-term bank loans	4(e), 7	126,353	—
Long-term deferred tax liabilities (including long-term deferred tax liabilities of consolidated VIEs without recourse to the Company of \$3,846 and \$3,777, respectively)		7,824	12,334
Long-term contingent consideration (including long-term contingent consideration of consolidated VIEs without recourse to the Company of \$nil and \$4,162, respectively)	4(n)	—	4,162
<b>Total liabilities</b>		<b>444,818</b>	<b>671,696</b>
<b>Commitments and contingencies</b>	27		
<b>Mezzanine equity</b>			
<b>Total mezzanine equity</b>	19	<b>61,810</b>	<b>—</b>



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CHANGYOU.COM LIMITED

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		As of December 31,	
	Notes	2012	2013
		US\$	US\$
Shareholders' equity:			
Class A ordinary shares par value \$0.01, 200,000 authorized; 21,494 and 23,184, respectively, issued and outstanding as of December 31, 2012 and 2013		215	244
Class B ordinary shares par value \$0.01, 97,740 authorized; 84,290 and 82,490, respectively, issued and outstanding as of December 31, 2012 and 2013		843	825
Additional paid-in capital		88,626	92,066
Treasury shares (nil and 1,181 shares, respectively, as of December 31, 2012 and 2013)	25	—	(17,240)
Statutory reserves	22	9,351	9,367
Retained earnings		470,717	739,343
Accumulated other comprehensive income		38,133	71,733
Total Changyou.com Limited shareholders' equity		607,885	896,338
Non-controlling interest		—	17,178
Total shareholders' equity		607,885	913,516
Total liabilities, mezzanine equity and shareholders' equity		1,114,513	1,585,212

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



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CHANGYOU.COM LIMITED

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE YEARS ENDED DECEMBER 31, 2011, 2012 and 2013

(In thousands, except per share or per ADS data)

	Note	For the Year Ended December 31		
		2011 US\$	2012 US\$	2013 US\$
<b>Revenues:</b>				
Online game		435,512	570,346	669,168
Online advertising		36,349	42,525	49,998
IVAS		1,862	4,307	5,402
Others		10,853	6,251	13,307
<b>Total revenues</b>		<b>484,576</b>	<b>623,429</b>	<b>737,875</b>
<b>Cost of revenues:</b>				
Online game		49,837	76,432	93,306
Online advertising (including transactions with a related party of \$37, \$50 and \$373, respectively)		3,892	6,535	13,827
IVAS		—	1,509	1,786
Others (including transactions with a related party of \$763, \$1,552 and \$1,310, respectively)		13,783	20,046	17,518
<b>Total cost of revenues</b>		<b>67,512</b>	<b>104,522</b>	<b>126,437</b>
<b>Gross profit</b>		<b>417,064</b>	<b>518,907</b>	<b>611,438</b>
<b>Operating expenses:</b>				
Product development		52,238	73,755	119,909
Sales and marketing (including transactions with a related party of \$6,002, \$14,026 and \$13,390, respectively)		49,893	60,639	128,830
General and administrative (including transactions with a related party of \$1,483, \$27 and \$12, respectively)		29,684	33,514	57,191
Goodwill impairment and impairment of acquired intangibles via acquisition of businesses		5,420	2,906	—
<b>Total operating expenses</b>		<b>137,235</b>	<b>170,814</b>	<b>305,930</b>
<b>Operating profit</b>		<b>279,829</b>	<b>348,093</b>	<b>305,508</b>
Interest income		11,933	15,882	28,455
Foreign currency exchange loss		(618)	(558)	(5,936)
Interest expense		(7)	(2,243)	(8,835)
Other income (expense)		457	(173)	3,613
<b>Income before income tax expense</b>		<b>291,594</b>	<b>361,001</b>	<b>322,805</b>
Income tax expense	20	43,580	67,405	36,383
<b>Net income</b>		<b>248,014</b>	<b>293,596</b>	<b>286,422</b>
Less: Net income attributable to the mezzanine classified non-controlling interest		2,558	11,196	17,780
<b>Net income attributable to Changyou.com Limited</b>		<b>245,456</b>	<b>282,400</b>	<b>268,642</b>
<b>Net income</b>		<b>248,014</b>	<b>293,596</b>	<b>286,422</b>
Other comprehensive income: Foreign currency translation adjustment		21,867	3,385	33,600
<b>Comprehensive income</b>		<b>269,881</b>	<b>296,981</b>	<b>320,022</b>
Comprehensive income attributable to the mezzanine classified non-controlling interest		2,558	11,196	17,780
<b>Comprehensive income attributable to Changyou.com Limited</b>		<b>267,323</b>	<b>285,785</b>	<b>302,242</b>
Basic net income per share	23	2.34	2.67	2.53
Diluted net income per share	23	2.30	2.64	2.52
Basic net income per ADS		4.68	5.35	5.06
Diluted net income per ADS		4.61	5.29	5.04
Weighted average number of ordinary shares outstanding, basic		104,854	105,656	106,252
Weighted average number of ordinary shares outstanding, diluted		106,600	106,792	106,676
Weighted average number of ADS outstanding, basic		52,427	52,828	53,126
Weighted average number of ADS outstanding, diluted		53,300	53,396	53,338
<b>Total share-based compensation cost included in:</b>				
Cost of revenues		230	306	101
Product development		2,399	1,854	475
Sales and marketing		960	326	74
General and administrative		2,528	1,183	624

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



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CHANGYOU.COM LIMITED

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2011, 2012 and 2013

(In thousands)

	Ordinary shares								
	Number of shares	Amount US\$	Additional paid-in capital US\$	Treasury shares US\$	Statutory reserves US\$	Retained earnings US\$	Accumulated other comprehensive income US\$	Non- controlling interest US\$	Total shareholders' equity US\$
<b>Balance as of December 31, 2010</b>	104,078	1,041	83,609	—	5,748	324,227	12,881	—	427,506
Issuance of ordinary shares upon vesting and settlement of restricted share units	945	9	(9)	—	—	—	—	—	—
Share-based compensation	—	—	5,547	—	—	—	—	—	5,547
Share-based compensation allocated from Sohu	—	—	570	—	—	—	—	—	570
Foreign currency translation adjustment	—	—	—	—	—	—	21,867	—	21,867
Appropriation to statutory reserves	—	—	—	—	3,603	(3,603)	—	—	—
Net income attributable to Changyou.com Limited	—	—	—	—	—	245,456	—	—	245,456
Deemed dividend distribution to Sohu (related to the 17173 Business)*	—	—	(11,589)	—	—	(30,116)	—	—	(41,705)
Deemed dividend distribution to Sohu	—	—	—	—	—	(141,996)	—	—	(141,996)
Transaction costs related to acquisition of the 17173 Business	—	—	—	—	—	(2,384)	—	—	(2,384)
<b>Balance as of December 31, 2011</b>	105,023	1,050	78,128	—	9,351	391,584	34,748	—	514,861
Issuance of ordinary shares upon vesting and settlement of restricted share units	761	8	(8)	—	—	—	—	—	—
Share-based compensation	—	—	3,366	—	—	—	—	—	3,366
Share-based compensation allocated from Sohu	—	—	303	—	—	—	—	—	303
Foreign currency translation adjustment	—	—	—	—	—	—	3,385	—	3,385
Net income attributable to Changyou.com Limited	—	—	—	—	—	282,400	—	—	282,400
Dividend distribution to shareholders	—	—	—	—	—	(200,875)	—	—	(200,875)
Contribution from mezzanine equity holder (see Note 19)	—	—	6,837	—	—	—	—	—	6,837
Deemed dividend distribution to Sohu (related to the 17173 Business)**	—	—	—	—	—	(2,392)	—	—	(2,392)
<b>Balance as of December 31, 2012</b>	105,784	1,058	88,626	—	9,351	470,717	38,133	—	607,885
Issuance of ordinary shares upon vesting and settlement of restricted share units	1,071	11	(11)	—	—	—	—	—	—
Share-based compensation	—	—	1,117	—	—	—	—	—	1,117
Share-based compensation allocated from Sohu	—	—	77	—	—	—	—	—	77
Foreign currency translation adjustment	—	—	—	—	—	—	33,600	—	33,600
Net income attributable to Changyou.com Limited	—	—	—	—	—	268,642	—	—	268,642
Appropriation for statutory reserves	—	—	—	—	16	(16)	—	—	—
Gain from acquisition of minority interest in 7Road***	—	—	2,409	—	—	—	—	—	2,409
Transaction costs for acquisition of minority interest in 7Road	—	—	(152)	—	—	—	—	—	(152)
Repurchase of common stock	—	—	—	(17,240)	—	—	—	—	(17,240)
Acquisition of majority interest in Raidcall Business****	—	—	—	—	—	—	—	17,178	17,178
<b>Balance as of December 31, 2013</b>	106,855	1,069	92,066	(17,240)	9,367	739,343	71,733	17,178	913,516

\* The Group acquired from Sohu certain, but not all, assets and liabilities associated with the 17173 Business. Current assets and liabilities associated with the 17173 Business as of December 15, 2011 that were not transferred to the Group are accounted for as a deemed dividend distribution to Sohu.

\*\* Represents revenues of the 17173 Business recognized in 2012, for which the related cash was received and retained by Sohu before the 17173 Business was acquired from Sohu in December 2011.

\*\*\* The gain represents the excess of the carrying value of the non-controlling interest over the consideration for the Group's acquisition of the minority interests in 7Road.

\*\*\*\* The Group acquired 62.5% of the equity interests, on a fully-diluted basis, in TalkTalk on December 24, 2013. Beijing Kunlun Tech Co., Ltd. and certain of its affiliates (collectively, the "Kalends Group") continued to hold 22.5% of the equity interests in TalkTalk on a fully-diluted basis. The non-controlling interest consists primarily of the interests in TalkTalk held by the Kalends Group.



**CHANGYOU.COM LIMITED**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2011, 2012 AND 2013**  
**(In thousands)**

	For the Year Ended December 31,		
	2011	2012	2013
	US\$	US\$	US\$
<b>Cash flows from operating activities:</b>			
<b>Net income</b>	248,014	293,596	286,422
Adjustments to reconcile net income to net cash provided by operating activities			
Bad debt provision	1,897	1,108	(300)
Depreciation	11,140	14,557	15,583
Amortization of intangible assets	17,652	23,416	26,790
Impairment loss of goodwill and intangible assets	6,524	8,647	3,624
Share-based compensation allocated from Sohu	570	303	77
Share-based compensation expense	5,547	3,366	1,197
Loss from equity investments	994	—	850
Disposal loss of fixed assets and intangible assets	596	330	128
Deferred tax (credits) expenses	(1,462)	9,718	5,382
Change of contingent consideration	822	2,195	167
Interest income	—	(1,609)	(2,292)
Others	—	737	—
Changes in current assets and liabilities, net of acquisition:			
Accounts receivable, net	(2,355)	(12,989)	(11,843)
Prepaid and other current assets	7,794	(12,047)	(29,964)
Due from Sohu	(47,492)	(495)	102
Other assets, net	(772)	(11,293)	4,209
Accounts payable	(615)	7,369	22,751
Receipts in advance and deferred revenue	14,931	(9,651)	1,003
Due to Sohu	15,053	(4,962)	—
Accrued salary and benefits	4,233	8,567	15,825
Accrued liabilities to suppliers	(2,047)	3,830	5,922
Tax payables	(1,570)	8,079	13,352
Other accrued liabilities	(2,852)	7,664	(342)
<b>Net cash provided by operating activities</b>	<u>276,602</u>	<u>340,436</u>	<u>358,643</u>
<b>Cash flows from investing activities:</b>			
Purchase of fixed assets	(20,620)	(11,716)	(61,582)
Purchase of intangible assets and other assets	(16,857)	(22,740)	(34,141)
Cash paid relating to restricted time deposits	—	(244,609)	(168,635)
Prepayment for an office building	(62,848)	—	—
Cash paid for business acquisition, net of cash acquired	(216,611)	(945)	(109,695)
Investment in equity investees	(350)	(500)	—
Purchase of /proceeds from short-term investments, net	637	(32,617)	51,185
Other activities relating to investing activities	—	(1,569)	175
<b>Net cash used in investing activities</b>	<u>(316,649)</u>	<u>(314,696)</u>	<u>(322,693)</u>
<b>Cash flows from financing activities:</b>			
Proceeds of loans from offshore banks	—	239,353	167,000
Payment of contingent consideration	—	(13,106)	(19,658)
Payment for repurchase of shares	—	—	(17,240)
Dividend distributed to shareholders	—	(200,875)	—
Repayment of note payable to Sohu	—	(16,000)	—
Other cash payments relating to financing activities	—	(633)	—
<b>Net cash provided by financing activities</b>	<u>—</u>	<u>8,739</u>	<u>130,102</u>
<b>Effect of exchange rate changes on cash and cash equivalents</b>	<u>19,431</u>	<u>1,749</u>	<u>15,793</u>
<b>Net (decrease) increase in cash and cash equivalents</b>	<u>(20,616)</u>	<u>36,228</u>	<u>181,845</u>
<b>Cash and cash equivalents, beginning of year</b>	<u>351,027</u>	<u>330,411</u>	<u>366,639</u>
<b>Cash and cash equivalents, end of year</b>	<u>330,411</u>	<u>366,639</u>	<u>548,484</u>
<b>Supplemental disclosures of cash flow</b>			
Cash paid for income taxes	(38,116)	(52,976)	(48,590)
Cash paid for interest expense	—	(1,992)	(8,812)
<b>Supplemental schedule of non-cash investing activity</b>			
Consideration payable for the acquisition of 7Road	29,810	—	—
Consideration payable for the purchase of non-controlling interest in 7Road	—	—	2,000
Consideration payable for the acquisition of Doyo	—	—	4,952
Notes payable to Sohu	16,007	—	—
Changes in government grant in prepaid and other current assets	—	2,378	1,355
Purchase of fixed assets with proceeds released from restricted cash account	—	1,583	—
<b>Supplemental schedule of non-cash financing activity</b>			
Deemed dividend to Sohu related to the 17173 Business	41,705	2,392	—
Accrued professional fees in relation to initial public offering of 7Road	—	1,037	—

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



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## CHANGYOU.COM LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 1. ORGANIZATION AND NATURE OF OPERATIONS

The accompanying consolidated financial statements include the financial statements of Changyou.com Limited (the “Company” or “Changyou”) and its subsidiaries and variable interest entities (“VIEs”). The Company was incorporated in the Cayman Islands on August 6, 2007. The Company and its subsidiaries and VIEs are collectively referred to as the “Group”. The major subsidiaries and VIEs through which the Company conducts its business operations as of December 31, 2013 are described below:

Name of entity	Place and date of incorporation or acquisition	Effective interest held
<b>Controlled entities:</b>		
Changyou.com (HK) Limited (“Changyou HK”)	Hong Kong, China, August 13, 2007	100%
Beijing AmazGame Age Internet Technology Co., Ltd. (“AmazGame”)	Beijing, China, September 26, 2007	100%
Changyou.com (US), LLC. (“Changyou US”)	Delaware, United States of America, January 26, 2009	100%
Changyou.com (UK) Co., Ltd. (“Changyou UK”)	London, United Kingdom of Great Britain, July 3, 2009	100%
Changyou My Sdn. Bhd (“Changyou Malaysia”)	Kuala Lumpur, Malaysia, September 10, 2009	100%
Beijing Changyou Gamespace Software Technology Co., Ltd. (“Gamespace”)	Beijing, China, October 29, 2009	100%
Changyou.com Korea Limited (“Changyou Korea”)	Seoul, Korea, January 7, 2010	100%
Beijing Yang Fan Jing He Information Consulting Co., Ltd. (“Yang Fan Jing He”)	Beijing, China, April 22, 2010	100%
Changyou.com India Private Limited (“Changyou India”)	Maharashtra, India, March 11, 2011	100%
Changyou IT Services Trade Limited (“Changyou Turkey”)	Turkey, September 29, 2011	100%
ICE Entertainment (HK) Limited (“ICE HK”)	Hong Kong, China, acquired on May 28, 2010	100%
ICE Information Technology (Shanghai) Co., Ltd. (“ICE Information”)	Shanghai, China, acquired on May 28, 2010	100%
Shanghai Jing Mao Culture Communication Co., Ltd (“Shanghai Jingmao”)	Shanghai, China, acquired on January 25, 2011	100%
Beijing Changyou Jingmao Film & Culture Communication Co., Ltd. (“Beijing Jingmao”)	Beijing, China, acquired on January 25, 2011	100%
Shanghai Hejin Data Consulting Co., Ltd (“Shanghai Hejin”)	Shanghai, China, acquired on January 25, 2011	100%
Changyou.com Gamepower (HK) Limited (“Gamepower HK”)	Hong Kong, China, September 8, 2011	100%
Changyou.com Webgames (HK) Limited (“Webgames HK”)	Hong Kong, China, September 21, 2011	100%
7Road.com Limited (“7Road Cayman”)	Cayman Islands, incorporated on June 15, 2011	100%
7Road.com HK Limited (“7Road HK”)	Hong Kong, China, incorporated on July 6, 2011	100%
Shenzhen 7Road Network Technologies Co., Ltd. (“7Road Technology”)	Shenzhen, China, incorporated on December 1, 2011	100%
Kylie Enterprises Limited (“Kylie”)	British Virgin Islands, acquired on December 15, 2011	100%
Changyou.com Gamestar (HK) Limited (“Gamestar HK”)	Hong Kong, China, July 12, 2013	100%
Mobogarden Enterprises Limited (“Mobogarden”)	British Virgin Islands, incorporated on September 25, 2013	100%
Heroic Vision Holdings Limited (“Heroic”)	British Virgin Islands, incorporated on October 23, 2013	100%
TalkTalk Limited (“TalkTalk”)	British Virgin Islands, acquired on December 24, 2013	73.5%



Name of entity	Place and date of incorporation or acquisition	Effective interest held
<b>RaidCall (HK) Limited (“RaidCall HK”)</b>	Hong Kong, China, incorporated on November 26, 2013	73.5%
<b>Beijing Changyou RaidCall Internet Technology Co., Ltd. (“Changyou RaidCall”)</b>	Beijing, China, incorporated on December 9, 2013	73.5%
<b>VIEs:</b>		
<b>Beijing Gamease Age Digital Technology Co., Ltd. (“Gamease”)</b>	Beijing, China, incorporated on August 23, 2007	100%
<b>Shanghai ICE Information Technology Co., Ltd. (“Shanghai ICE”)</b>	Shanghai, China, acquired on May 28, 2010	100%
<b>Beijing Guanyou Gamespace Digital Technology Co., Ltd. (“Guanyou Gamespace”)</b>	Beijing, China, incorporated on August 5, 2010	100%
<b>Shenzhen 7Road Technology Co., Ltd. (“Shenzhen 7Road”)</b>	Shenzhen, China, acquired on May 11, 2011	100%
<b>Beijing Doyo Internet Technology Co., Ltd. (“Doyo”)</b>	Beijing, China, acquired on November 26, 2013	100%
<b>Beijing Changyou e-pay Co. Ltd. (“Changyou e-pay”)</b>	Beijing, China, incorporated on December 19, 2013	100%

The Group principally engages in the development, operation and licensing of massively multi-player online games (“MMOGs”), Web games and mobile games. The Group also engages in the online advertising business through its ownership and operation of a game information portal on the 17173.com Website. The Group’s principal operations and geographic market are in the People’s Republic of China (the “PRC”).

On April 7, 2009, the Company completed an initial public offering on the NASDAQ Global Select Market. In the offering, 8,625,000 American depositary shares (“ADSs”), representing 17,250,000 Class A ordinary shares, were sold to the public at a price of \$16.00 per ADS. Of these, 3,750,000 ADSs, representing 7,500,000 Class A ordinary shares, were sold by the Company; and 4,875,000 ADSs, representing 9,750,000 Class A ordinary shares, were sold by an indirect wholly-owned subsidiary of Sohu.com Inc. (“Sohu.com”). The net proceeds to the Company from the initial public offering, after deducting commissions and offering expenses, were approximately \$54.7 million.

## 2. REORGANIZATION, SHARE SPLIT AND ACQUISITIONS

### a. Reorganization

In August 2007, Sohu.com, which is the Company’s ultimate parent company, undertook a restructuring and reorganization (the “Reorganization”). Sohu.com and its subsidiaries and VIEs, excluding the Company and its subsidiaries and VIEs, are collectively referred to as “Sohu.” Sohu.com and its subsidiaries and VIEs, including the Company and its subsidiaries and VIEs, are collectively referred to as the “Sohu Group.” The Reorganization was effected in connection with a contemplated initial public offering by the Company on the NASDAQ Global Select Market.

Prior to the establishment of the Group, the operation and licensing of MMOGs were carried out by various companies owned or controlled by Sohu.com (the “Predecessor Operations”). In connection with the Reorganization, the Predecessor Operations, which include all operating assets and liabilities relating to the operation of massively multi-player online role-playing games (“MMORPGs”) (which are a subset of MMOGs), were transferred to the Group with legal effect as of December 1, 2007.

### b. Share Split and Issuances

(i) In May 2008, the Company effected a share split of each \$1.00 par value share into 100 shares of \$0.01 par value each, resulting in 5,000,000 ordinary shares authorized, issued and outstanding.

In May 2008, the Company’s authorized share capital was increased from 5,000,000 to 10,000,000 ordinary shares with a par value of \$0.01 per ordinary share, and in June 2008 the Company issued to Sohu.com (Game) Limited an additional 3,500,000 ordinary shares, such that Sohu.com (Game) Limited then held an aggregate of 8,500,000 ordinary shares, then representing 100% of the outstanding share capital of the Company.

(ii) In December 2008, the Company effected the following transactions: (a) Sohu.com (Game) Limited transferred 8,500,000 ordinary shares to the Company for cancellation; (b) the Company increased its authorized ordinary shares from 10,000,000 to 109,774,000 ordinary shares, par value \$0.01 per share, with 100,000,000 of such shares designated as Class A ordinary shares and 9,774,000 of such shares designated as Class B ordinary shares; and (c) the Company issued 8,000,000 Class B ordinary shares to Sohu.com (Game) Limited.



(iii) On March 16, 2009, the Company increased its authorized ordinary shares from 109,774,000 to 297,740,000 ordinary shares, par value \$0.01 per share, with 200,000,000 of such shares designated as Class A ordinary shares and 97,740,000 of such shares designated as Class B ordinary shares, and effected a ten-for-one split of outstanding Class B ordinary shares by way of a bonus share issuance of nine Class B ordinary shares for each Class B ordinary share then outstanding.

The impact of the share splits and issuances is accounted for retroactively in the periods presented herein.

#### ***c. Acquisition of the 17173 Business***

On December 15, 2011, the Group completed the acquisition from Sohu of certain assets and business operations associated with the online game information portal 17173.com Website (the “17173 Business”) for fixed cash consideration of approximately \$162.5 million. Under the acquisition agreement, the net profit of \$1.3 million generated from the Group’s operation of the 17173 Business during the transition period from December 16, 2011 through December 31, 2011 (the “Transition Period”) was for the benefit of Sohu. The Company accounted for this \$1.3 million as part of the consideration for the acquisition. See Note 6 – “BUSINESS COMBINATIONS –Acquisition of the 17173 Business” and Note 26 – “RELATED PARTY TRANSACTIONS.”

Because Changyou and the 17173 Business are under common control by Sohu, in accordance with ASC subtopic 805-50 the Company’s consolidated financial statements for the years ended December 31 2011 have been prepared as if the current corporate structure had been in existence throughout the periods presented.

#### ***d. Acquisition and Restructuring of 7Road***

On May 11, 2011, the Group, through its VIE Gamease, acquired 68.258% of the equity interests of Shenzhen 7Road and began to consolidate Shenzhen 7Road’s financial statements on June 1, 2011. Effective June 26, 2012, Shenzhen 7Road was reorganized into a Cayman Islands holding company structure (the “7Road Reorganization”) where Changyou holds a direct ownership interest in 7Road Cayman (together with its subsidiaries and variable interest entity, “7Road”) through the Group’s subsidiary Webgames HK and Shenzhen 7Road is a VIE of 7Road. As the reorganization did not result in any change in the ultimate beneficial ownership of Shenzhen 7Road’s business, assets and results of operations, the Group’s management believes that the reorganization should be viewed as a non-substantive transaction and treated as if it had been effective upon the Group’s acquisition of 68.258% of the equity interests in Shenzhen 7Road.

On June 21, 2012, 7Road Cayman’s then Chief Executive Officer surrendered to 7Road Cayman, without consideration, ordinary shares of 7Road Cayman representing 5.1% of the then outstanding ordinary shares of 7Road Cayman, with the intention that these shares would be added to the shares reserved by 7Road Cayman for grants of equity incentive awards under the 7Road 2012 Share Incentive Plan, without dilution of the other shareholders of 7Road Cayman. As a result, the non-controlling interest decreased to 28.074% of 7Road Cayman and the Group’s interest in 7Road Cayman increased to 71.926%. See Note 19 – “MEZZANINE EQUITY.”

On May 1, 2013, Changyou entered into an agreement to acquire all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders, representing 28.074% of the outstanding share capital of 7Road Cayman, and all of the equity interests in Shenzhen 7Road held by shareholders other than Gamease, for aggregate cash consideration of approximately \$78 million. Upon the closing of the acquisition on June 5, 2013, 7Road Cayman became an indirect wholly-owned subsidiary of Changyou, and Changyou’s VIE Gamease became the sole shareholder of 7Road’s VIE Shenzhen 7Road. As of December 31, 2013, Changyou had paid \$76 million of the total cash consideration. The remaining \$2 million will be settled in June 2014.

#### ***e. Acquisition of Doyo***

Beijing Doyo Internet Technology Co., Ltd, which is primarily engaged in the online advertising and traffic monetization business, was acquired by Guanyou Gamespace on November 26, 2013 for fixed cash consideration of approximately \$6.5 million and contingent consideration of up to \$7.3 million. As of December 31, 2013, the registered capital of Doyo was \$1.6 million and Guanyou Gamespace held 100% of the equity interests of Doyo.



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***f. Acquisition of the RaidCall Business***

On November 19, 2013, the Company entered into an investment agreement with the Kalends Group, pursuant to which TalkTalk was incorporated in the British Virgin Islands and initially wholly-owned by the Kalends Group, RaidCall HK was incorporated in Hong Kong as a wholly-owned subsidiary of TalkTalk, and Changyou RaidCall was incorporated in the PRC as a wholly-owned subsidiary of RaidCall HK. The Kalends Group then transferred to RaidCall HK and Changyou RaidCall all of the assets associated with a free social communication software platform, which is specifically designed for online gaming and music-related value-added services, that the Kalends Group operated through a series of Websites (the “RaidCall Business”). On December 24, 2013, pursuant to the investment agreement, the Company acquired 62.5% of the equity interests, on a fully-diluted basis, in TalkTalk for cash consideration of \$ 47.6 million. Of the total consideration, \$27.6 million was paid to purchase from the Kalends Group a portion of the ordinary shares of TalkTalk held by the Kalends Group, and \$20 million was injected for newly-issued ordinary shares of TalkTalk. Also effective upon the closing of the transaction, 15% of the equity interests of TalkTalk on a fully-diluted basis were reserved for grants of equity incentive awards to key employees of the RaidCall Business and the Kalends Group continued to hold the remaining 22.5% of the equity interests on a fully-diluted basis.

At the closing of the transaction, the parties entered into a shareholder agreement pursuant to which the Company has the right to designate three of the five directors of TalkTalk, including the chairman of the board, and the Company has customary rights of first refusal with respect to proposed transfers of equity interests in TalkTalk by the Kalends Group. The shareholder agreement also specifies that if TalkTalk fails to achieve specified performance milestones for the month of December 2014, then the Kalends Group, any key employees of the RaidCall Business who hold equity interests in TalkTalk, and, under certain circumstances, TalkTalk will be required to transfer to the Company, without consideration, equity interests in TalkTalk in amounts sufficient to cause the Company’s equity interests to increase to 70% on a fully-diluted basis.

**3. VARIABLE INTEREST ENTITIES*****Consolidated VIEs******Basic Information***

PRC law and regulations prohibit or restrict foreign ownership of companies that operate online games and internet content services. Consequently, the Group operates its online game business and online advertising business through the VIEs. Both Gamease and Guanyou Gamespace are directly owned by the Company’s Chief Executive Officer (“CEO”) and Dewen Chen, the Company’s President (the “President”), who hold 60% and 40%, respectively, of each of these entities. Shanghai ICE is owned by two Changyou employees, Runa Pi and Rong Qi, each of whom holds 50% of Shanghai ICE. Capital for the VIEs is funded by the Company through loans provided to the Company’s CEO and President and Ms. Pi and Ms. Qi, and the loans are initially recorded as loans to related parties. Guanyou Gamespace owns 100% of the equity interests of Doyo.

The loans to the shareholders of Gamease, Guanyou Gamespace, and Shanghai ICE and the capital of the VIEs are eliminated for accounting purposes during consolidation.

Under contractual agreements with the Company, shareholders of Gamease, Guanyou Gamespace and Shanghai ICE are required to transfer their ownership in Gamease, Guanyou Gamespace and Shanghai ICE to the Company, if permitted by PRC law and regulations, or, if not so permitted, to designees of the Company at any time to repay the loans outstanding. All voting rights of Gamease, Guanyou Gamespace and Shanghai ICE are assigned to the Company; the Company has the right to designate all directors and senior management personnel of Gamease, Guanyou Gamespace and Shanghai ICE. The Company’s CEO and President and the two Changyou employees have pledged their shares in Gamease, Guanyou Gamespace and Shanghai ICE as collateral for the loans. As of December 31, 2012 and 2013, the aggregate amount of these loans was \$3,802,000 and \$3,920,000, respectively.

Effective upon the completion of the 7Road Reorganization, Shenzhen 7Road became a VIE of 7Road Cayman, of which approximately 71.926% was owned by Changyou through Webgames HK. Shenzhen 7Road was directly owned by Changyou’s VIE Gamease, which held 68.258%, and by the other shareholders of Shenzhen 7Road, who held 31.742%. On June 5, 2013, Changyou, through Webgames HK, acquired all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders of 7Road Cayman and, through Gamease, acquired all of the equity interests in Shenzhen 7Road held by shareholders other than Gamease. See Note 2.d “–Acquisition and Restructuring of 7Road.” The Company is a primary beneficiary of Shenzhen 7Road, as a result of contractual arrangements among Shenzhen 7Road, 7Road Technology and Gamease.



The Group has adopted the guidance of accounting for variable interest entities, which requires certain variable interest entities to be consolidated by the primary beneficiary of the entity. The Group's management evaluated the relationships between the Company, AmazGame and Gamease, the relationships between the Company, Gamespace and Guanyou Gamespace, the relationships between the Company, ICE Information and Shanghai ICE, the relationship between the Company, 7Road Technology and Shenzhen 7Road, and the economic benefit flow of the applicable contractual arrangements. In connection with such evaluation, management also took into account the fact that AmazGame, Gamespace, ICE Information and 7Road Technology, as a result of the above contractual arrangements, control 100% of the shareholders' voting interests in Gamease, Guanyou Gamespace, Shanghai ICE and Shenzhen 7Road and the fact that Guanyou Gamespace, in turn, holds and controls 100% of the shareholder's voting interests in Doyo. The Group concluded that each of Gamease, Guanyou Gamespace, Shanghai ICE, Shenzhen 7Road, Doyo and Changyou e-pay is a variable interest entity of the Company, of which the Company is the primary beneficiary. As a result, Gamease's, Guanyou Gamespace's, Shanghai ICE's, Shenzhen 7Road's, Doyo's and Changyou e-pay's results of operations, assets and liabilities have been included in the Group's consolidated financial statements.

### Financial Information

The following combined financial information of the Group's VIEs was included in the accompanying consolidated financial statements of the Group as follows:

	As of December 31, (in thousands)	
	2012	2013
<b>ASSETS:</b>		
Cash and cash equivalents	\$ 57,517	\$107,356
Short-term investments	51,720	—
Accounts receivable, net	21,610	31,245
Prepaid expense	782	1,659
Other receivable	26,061	19,843
Due from affiliates	102,300	223,485
Due from Sohu Group	431	392
Others	2,219	1,826
Total current assets	262,640	385,806
Goodwill	116,992	128,139
Deferred tax assets and provision	777	479
Other non-current assets	49,956	91,929
Total assets	\$430,365	\$606,353
<b>LIABILITIES:</b>		
Accounts payable	\$ 8,677	\$ 25,986
Accrued and other short-term liabilities	38,033	21,160
Due to affiliates	36,446	226,510
Receipts in advance and deferred revenue	43,027	43,252
Tax payable	9,923	1,453
Total current liabilities	136,106	318,361
Other long-term liabilities	3,846	7,939
Total liabilities	\$139,952	\$326,300

	For the Year ended December 31, (in thousands)		
	2011	2012	2013
Net revenue	\$434,018	\$613,629	\$719,253
Net income (loss)	50,683	99,276	(1,170)

	For the Year ended December 31, (in thousands)		
	2011	2012	2013
Net cash provided by operating activities	\$ 56,622	\$ 66,739	\$102,086
Net cash used in investing activities	(80,971)	(43,087)	(53,925)
Net cash used in financing activities	—	(13,106)	—



Under contractual arrangements with the VIEs, the Company has the power to direct activities of the VIEs, and can have assets transferred freely out of the VIEs without any restrictions. Therefore, the Company considers that there is no asset of the consolidated VIEs that can be used only to settle obligations of the VIEs, except for registered capital and PRC statutory reserves of the VIEs. As of December 31, 2013, the registered capital and PRC statutory reserves of the VIEs totaled \$12.8 million. As the consolidated VIEs are incorporated as limited liability companies under the PRC Company Law, creditors of the consolidated VIEs do not have recourse to the general credit of the Company for any of the liabilities of such VIEs.

Currently there is no contractual arrangement that requires the Company to provide additional financial support to the VIEs. As the Company is conducting its online game business and online advertising business mainly through the VIEs, the Company may provide such support on a discretionary basis in the future, which could expose the Company to a loss.

Summary of significant agreements currently in effect

Agreements between VIEs and Nominee Shareholders

*Loan agreements and equity pledge agreements* between AmazGame and the shareholders of Gamease and between Gamespace and the shareholders of Guanyou Gamespace. The loan agreements provide for loans to the respective shareholders of Gamease and Guanyou Gamespace for the shareholders to make contributions to the registered capital of Gamease and Guanyou Gamespace in exchange for the equity interests in Gamease and Guanyou Gamespace. Under the equity pledge agreements, the respective shareholders of Gamease and Guanyou Gamespace pledge to AmazGame and Gamespace, their equity interests in Gamease and Guanyou Gamespace to secure the performance of their obligations under the loan agreements and Gamease's and Guanyou Gamespace's obligations to AmazGame and Gamespace under the various VIE-related agreements. The loans are interest free and are repayable on demand, but the shareholders can only repay the loans by transferring to AmazGame and Gamespace, as the case may be, their equity interests in Gamease and Guanyou Gamespace.

*Equity interest purchase right agreements* between AmazGame and the shareholders of Gamease and between Gamespace and the shareholders of Guanyou Gamespace. Pursuant to these agreements, AmazGame and Gamespace have the right, exercisable at any time when it becomes legal to do so under PRC law, to purchase from the respective shareholders of Gamease and Guanyou Gamespace all or any part of their equity interests at a purchase price equal to their initial contributions to registered capital.

*Powers of attorney* executed by the shareholders of Gamease in favor of AmazGame and by the shareholders of Guanyou Gamespace in favor of Gamespace, with a term of 10 years. These powers of attorney give AmazGame and Gamespace the exclusive right to appoint nominees to act on behalf of their respective shareholders in connection with all actions to be taken by Gamease and Guanyou Gamespace.

*Business operation agreements* between AmazGame and the shareholders of Gamease and between Gamespace and the shareholders of Guanyou Gamespace. These agreements set forth the right of AmazGame and Gamespace, to control the actions of the respective shareholders of Gamease and Guanyou Gamespace. Each agreement has a term of 10 years.

*Call option agreement* among ICE Information, Shanghai ICE and Shanghai ICE shareholders. This agreement provides to ICE Information and any third party designated by ICE Information the right, exercisable at any time when it becomes legal to do so under PRC law, to purchase from the shareholders all or any part of their shares in Shanghai ICE or purchase from Shanghai ICE all or part of its assets or business at the lowest purchase price permissible under PRC law. The agreement further provides that Shanghai ICE or its shareholders will transfer back to ICE Information any such purchase price they have received from ICE Information, upon the request of ICE Information, as and to the extent allowed under PRC law. The agreement is terminable only if ICE Information is dissolved.

*Share pledge agreement* among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE. Under this agreement the shareholders pledge to ICE Information their equity interests in Shanghai ICE to secure the performance of their obligations under the call option agreement and to secure Shanghai ICE's obligations to ICE Information under their VIE-related agreements.

*Business operation agreement* among ICE Information, Shanghai ICE and the shareholders of Shanghai ICE. This agreement sets forth the right of ICE Information to control the actions of the shareholders of Shanghai ICE. The agreement is terminable only if ICE Information is dissolved.

*Amended and restated equity interest purchase right agreement* among 7Road Technology, Shenzhen 7Road and Gamease, which is Shenzhen 7Road's sole shareholder. Under this agreement, 7Road Technology and any third-party designated by 7Road Technology have the right, exercisable at any time during the term of the agreement, if and when it is legal to do so under PRC law, to purchase from Gamease all or any part of its shares in Shenzhen 7Road at a nominal purchase price. This agreement has a term of 10 years, is renewable by 7Road Technology for such term as it may determine and is terminable by 7Road Technology by notice to the other parties at any time when, under PRC law as then in effect, 7Road Technology cannot exercise its purchase right, and is also terminable if Shenzhen 7Road's or 7Road's existence is terminated, by mutual agreement of the parties or upon the written request of 7Road Technology. Neither Gamease nor Shenzhen 7Road has any power to terminate the agreement.



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*Amended and restated equity interest pledge agreement* among 7Road Technology, Shenzhen 7Road and Gamease. Under this agreement, Gamease agreed to pledge to 7Road Technology its equity interests in Shenzhen 7Road to secure the performance of Gamease's obligations and Shenzhen 7Road's obligations under the various VIE-related agreements. If Gamease or Shenzhen 7Road breaches its obligations under any VIE-related agreements, 7Road Technology is entitled to exercise its rights as the beneficiary under the Equity Interest Pledge Agreements. This agreement terminates only after all of the obligations of Gamease and of Shenzhen 7Road under the various VIE-related agreements are no longer in effect.

*Amended and restated business operation agreement* among 7Road Technology, Shenzhen 7Road and Gamease. This agreement grants to 7Road Technology the right to control the actions of Shenzhen 7Road and to control the actions of Gamease in its capacity as the sole shareholder of Shenzhen 7Road. This agreement has a term of 10 years, is renewable by 7Road Technology for such term as it may determine and is terminable early if the existence of Shenzhen 7Road or 7Road Technology is terminated or upon 30 days' advance written notice of 7Road Technology to Shenzhen 7Road.

*Powers of attorney* executed by Gamease in favor of 7Road Technology. This power of attorney gives 7Road Technology the exclusive right to appoint designees to act on behalf of Gamease in connection with all actions to be taken by Shenzhen 7Road requiring shareholder approval.

#### Business Arrangements Between WFOEs and VIEs

*Technology support and utilization agreements* between AmazGame and Gamease and between Gamespace and Guanyou Gamespace. Pursuant to these agreements, AmazGame and Gamespace have the exclusive right to provide certain product development and application services and technology support to Gamease and Guanyou Gamespace, respectively, for a fee equal to a predetermined percentage, subject to adjustment by AmazGame or Gamespace at any time, of Gamease's and Guanyou Gamespace's respective revenues. Each agreement terminates only when AmazGame or Gamespace is dissolved.

*Services and maintenance agreements* between AmazGame and Gamease between Gamespace and Guanyou Gamespace. Pursuant to these agreements, AmazGame and Gamespace, respectively, provide marketing, staffing, business operation and maintenance services to Gamease and Guanyou Gamespace, respectively, in exchange for a fee equal to the cost of providing such services plus a predetermined margin. Each agreement terminates only when AmazGame or Gamespace, as the case may be, is dissolved.

*Exclusive business cooperation agreement* between ICE Information and Shanghai ICE. This agreement sets forth the exclusive right of ICE Information to provide business support and technical services to Shanghai ICE. The agreement terminates only when ICE Information is dissolved.

*Exclusive technology consulting and services agreement* between ICE Information and Shanghai ICE. This agreement provides to ICE Information the exclusive right to provide technical consultation and other related services to Shanghai ICE in exchange for a fee equal to the balance of Shanghai ICE's gross income after deduction of related costs and expenses. The agreement terminates only when ICE Information is dissolved.

*Technology development and utilization agreement* between 7Road Technology and Shenzhen 7Road. Under this agreement, 7Road Technology has the exclusive right to provide product development and application services and technology support to Shenzhen 7Road for a fee based on Shenzhen 7Road's revenues, which fee can be adjusted by 7Road Technology at any time in its sole discretion. The fee is eliminated upon consolidation. This agreement will terminate if the existence of 7Road Technology or Shenzhen 7Road is terminated, by mutual agreement of the parties or upon failure to perform due to a force majeure event.

*Services and maintenance agreement* between 7Road Technology and Shenzhen 7Road. Pursuant to this agreement, 7Road Technology provides marketing and maintenance services to Shenzhen 7Road in exchange for a fee equal to the cost of providing such services plus a predetermined margin. This agreement will terminate if the existence of 7Road Technology or Shenzhen 7Road is terminated, by mutual agreement of the parties or upon failure to perform due to a force majeure event.

Certain of the agreements described above between the VIEs and the corresponding wholly-owned subsidiaries, or WFOEs, of the Company do not have renewal terms. However, because the VIEs are controlled by their corresponding WFOEs through their respective business operation agreements and through the powers of attorney granted to the WFOEs by the shareholders of the VIEs, such agreements can be, and are expected to be, renewed at the election of the WFOEs.



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***VIE-Related Risks***

It is possible that the Group's conduct of certain of its operations and businesses through VIEs could be found by PRC authorities to be in violation of PRC law and regulations prohibiting or restricting foreign ownership of companies that engage in such operations and businesses. If such a finding were made, regulatory authorities with jurisdiction over the licensing and operation of such operations and businesses would have broad discretion in dealing with such a violation, including levying fines, confiscating the Group's income, revoking the business or operating licenses of the affected businesses, requiring the Group to restructure its ownership structure or operations, or requiring the Group to discontinue all or any portion of its operations. Any of these actions could cause significant disruption to the Group's business operations, and have an adverse impact on the Group's cash flows, financial position and operating performance. The Group's management considers the possibility of such a finding by PRC regulatory authorities to be remote.

In addition, it is possible that the contracts among the Group, the Group's VIEs and shareholders of its VIEs would not be enforceable in China if PRC government authorities or courts were to find that such contracts contravene PRC law and regulations or are otherwise not enforceable for public policy reasons. In the event that the Group was unable to enforce these contractual arrangements, the Group would not be able to exert effective control over the affected VIEs. Consequently, such VIE's results of operations, assets and liabilities would not be included in the Group's consolidated financial statements. If such were the case, the Group's cash flows, financial position and operating performance would be impaired. The Group's contractual arrangements with respect to its consolidated VIEs are approved and in place. The Group's management believes that such contracts are enforceable, and considers the possibility remote that PRC regulatory authorities with jurisdiction over the Group's operations and contractual relationships would find the contracts to be unenforceable.

***Variable interest entities not consolidated within the Group***

In 2010, in order to diversify the Company's marketing channels for its games, the Company acquired a 50% equity interest in Shanghai Jingmao and its affiliate. Although following the acquisition Shanghai Jingmao and its affiliate were variable interest entities of the Company under generally accepted accounting principles in the United States of America ("U.S. GAAP"), the Company was not the primary beneficiary of Shanghai Jingmao and its affiliate because the Company was not able to direct their activities. Accordingly, the Company did not consolidate the financial statements of Shanghai Jingmao and its affiliate prior to February 1, 2011 and the Company's investment in them was accounted for under the equity method of accounting. In January 2011, the Company acquired the remaining 50% of the equity interests in each of Shanghai Jingmao and its affiliate, resulting in the Company's having control of 100% of the voting equity interests. Accordingly, the Company began to consolidate the financial statements of Shanghai Jingmao and its affiliate on February 1, 2011.

**4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES*****a. Basis of presentation and consolidation***

The consolidated financial statements have been prepared on a historical cost basis to reflect the financial position and results of operations of the Company in accordance with U.S. GAAP and on a going concern basis.

The consolidated financial statements include the financial statements of the Company and its controlled operating entities including the subsidiaries and the VIEs. All inter-company balances and transactions within the Group have been eliminated on consolidation.

The Company has adopted the guidance of accounting for VIEs, which requires VIEs to be consolidated by the primary beneficiary of the entity. The Company's management made evaluations of the relationships between the Company and its VIEs and the economic benefit flow of contractual arrangements with the VIEs. In connection with such evaluation, management also took into account the fact that, as a result of such contractual arrangements, the Group controls the shareholders' voting interests in the VIEs. As a result of such evaluation, management concluded that the Group is the primary beneficiary of its VIEs. As a result, the Company consolidates all of its VIEs in its consolidated financial statements. Please refer to Note 3 – "VARIABLE INTEREST ENTITIES" for more details.

Because of the Company's acquisition on December 15, 2011 of the 17173 Business, which is under common control by Sohu with the Company, the Company's consolidated financial statements as of and for the years ended December 31, 2011 incorporate the results of operations of the combining entities and businesses as to which the common control combination occurred as if the combining entities and businesses had been combined from the date when they first came under the control of Sohu, the controlling party.

Certain acquired assets of the combining entities and businesses were combined using the existing book values from the perspective of Sohu, the controlling party. No amount was recognized in consideration of goodwill or for the excess of Changyou's interest in the net fair value of the 17173 Business's identifiable assets, liabilities and contingent liabilities over cost at the time of the common control combination, to the extent of the continuation of Sohu's interest.



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ASC subtopic 805-50 provides that the consolidated statements of comprehensive income should include the results of each of the combining entities and businesses from the earliest date presented or, if more recent, from the date when the combining entities and businesses first came under common control, regardless of the date of the common control combination.

*Reclassification of revenues and costs related to Changyou Internet value-added services ("IVAS")*

Commencing January 1, 2013, in order to provide a better foundation for understanding the Group's performance, both revenues and costs generated from the operation of third-party Web games by the 17173 Business were reclassified from the online game business and the online advertising business to IVAS business. To conform to the current period presentations, the relevant amounts for prior periods have been reclassified accordingly. Such reclassifications amounted to \$4.3 million and \$1.9 million, respectively, for revenues and \$nil and \$1.5 million, respectively, for costs for the years ended December 31, 2011 and 2012.

**b. Use of estimates**

The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. Significant judgments and estimates include accounting for the basis of consolidation, the recognition of revenues, the determination of share-based compensation expense, the determination of the fair value of identifiable assets and liabilities acquired through business combination, the determination of the fair value of contingent consideration, the determination of the fair value of mezzanine equity, the determination of segment aggregation, assessment of income tax and valuation allowances against deferred tax assets, determination of allowance of doubtful accounts, assessment of impairment of intangible assets, fixed assets, other assets, equity investments and goodwill and the determination of functional currencies.

**c. Fair value measurement**

The Company's financial instruments include cash equivalents, restricted time deposits, accounts receivable, short-term investments, prepaid and other current assets, long-term prepayment and other non-current assets, short-term and long-term accounts payable, receipts in advance and deferred revenue, accrued liabilities to suppliers, short-term and long-term bank loans and other accrued liabilities. For fair value measurement, U.S. GAAP establishes a three-tier hierarchy which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1—observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2—other inputs that are directly or indirectly observable in the marketplace.

Level 3—unobservable inputs which are supported by little or no market activity.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

**d. Cash and cash equivalents**

The Company's cash equivalents mainly consist of time deposits placed with banks with an original maturity of three months or less.

**e. Restricted time deposits - Loans from offshore banks, secured by time deposits**

The loans from the offshore branches of the lending banks are classified as short-term bank loans or long-term bank loans based on their repayment periods. The rates of interest under the loan agreements with the lending banks were determined based on the prevailing interest rates in the market. The RMB onshore deposits securing the offshore loans are treated as restricted time deposits on the Company's consolidated balance sheets. Restricted time deposits are valued based on the prevailing interest rates in the market.

**f. Accounts receivable, net**

The carrying value of accounts receivable is reduced by an allowance that reflects the Company's best estimate of the amounts that will not be collected. The Company makes estimates of the collectability of accounts receivable. Many factors are considered in estimating the general allowance, including reviewing delinquent accounts receivable, performing aging analyses and customer credit analyses, and analyzing historical bad debt records and current economic trends. Additional allowance for specific doubtful accounts might be made if the Company's customers are unable to make payments due to their deteriorating financial conditions. As of December 31, 2012 and 2013, the provision for bad debts was \$3.1 million and \$2.7 million, respectively.





**g. Short-term investments**

In accordance with ASC 825, for investments in financial instruments with a variable interest rate indexed to the performance of underlying assets, the Company elected the fair value method at the date of initial recognition and carried these investments subsequently at fair value. Changes in the fair value are reflected in the consolidated statements of comprehensive income. To estimate fair value, the Company refers to the quoted rate of return provided by banks at the end of each period using the discounted cash flow method. Since these investments' maturity dates are within one year, they are classified as short-term investments. For the years ended December 31, 2011, 2012 and 2013, the Company recorded changes in the fair value of short-term investments in the consolidated statements of comprehensive income of \$659,000, \$1.5 million and \$2.5 million, respectively.

**h. Fixed assets and depreciation**

Fixed assets, comprising office buildings, computer equipment (including servers), and leasehold improvements are stated at cost less accumulated depreciation and impairment. Fixed assets are depreciated at rates sufficient to write off their costs less impairment, if any, over the estimated useful lives of the assets on a straight-line basis, with no residual value. The estimated useful lives are as follows:

	<u>Estimated useful life</u>
Office building	36-47 years
Computer equipment (including servers)	4 years
Leasehold improvements	Lesser of the term of the lease or the estimated useful lives of the assets
Building improvements	10 years
Office furniture	5 years
Vehicles	4-10 years

Expenditure for maintenance and repairs is expensed as incurred.

The gain or loss on the disposal of fixed assets is the difference between the net sales proceeds and the carrying amount of the relevant assets and is recognized in operating expenses in the consolidated statements of comprehensive income.

As of December 31, 2012 and 2013, the original costs of fully depreciated assets which are still in use were \$15.0 million and \$20.9 million, respectively.

**i. Intangible assets**

Intangible assets, comprising operating rights for licensed games, computer software purchased from unrelated third parties, developed technologies, trademarks and domain names, cinema advertising slot rights and other finite-lived intangible assets, which are separable from the fixed assets, are stated at cost less accumulated amortization. Amortization is computed using the straight-line method over the estimated useful lives of the assets.

**j. Equity investments**

Investments in entities over which the Company does not have significant influence are recorded as equity investments and are accounted for by the cost method. Investments in entities over which the Company has significant influence but does not control are also recorded as equity investments and are accounted for by the equity method. Under the equity method, the Company's share of the post-acquisition profits or losses of the equity investment is recognized in the Company's consolidated statements of comprehensive income; and the Company's share of post-acquisition movements in equity investments is recognized in equity in the Company's consolidated balance sheets. Unrealized gains on transactions between the Company and its equity investments are eliminated to the extent of the Company's interest in the equity investments. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. When the Company's share of losses in an equity investment equals or exceeds its interest in the equity investment, the Company does not recognize further losses, unless the Company has incurred obligations or made payments on behalf of the equity investee.

**k. Goodwill**

Goodwill represents the excess of the purchase price over the fair value of the identifiable assets and liabilities acquired as a result of the Company's acquisitions of interests in its subsidiaries and VIEs.



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The Company tests goodwill for impairment at the reporting unit level on an annual basis as of October 1, and between annual tests when an event occurs or circumstances change that could indicate that the asset might be impaired. Commencing in September 2011, in accordance with the FASB revised guidance on "Testing of Goodwill for Impairment," a company first has the option to assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the company decides, as a result of its qualitative assessment, that it is more-likely-than-not that the fair value of a reporting unit is less than its carrying amount, the quantitative impairment test is mandatory. Otherwise, no further testing is required. The quantitative impairment test consists of a comparison of the fair value of goodwill with its carrying value. Application of a goodwill impairment test requires significant management judgment, including the identification of reporting units, assigning assets and liabilities to reporting units, assigning goodwill to reporting units, and determining the fair value of each reporting unit. The judgment in estimating the fair value of reporting units includes estimating future cash flows, determining appropriate discount rates and making other assumptions. Changes in these estimates and assumptions could materially affect the determination of fair value for each reporting unit.

The Company acquired Doyo and the Raidcall Business in November and December 2013. Management was not aware of any significant events or circumstances that would be more likely than not to reduce the fair values of the reporting units below their carrying values.

If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss should be recognized in an amount equal to that excess. The goodwill impairment losses for the years ended December 31, 2011, 2012 and 2013 were \$5.2 million, \$nil and \$nil, respectively.

#### ***l. Impairment of long-lived assets and intangible assets***

The carrying amounts of long-lived assets and intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is evaluated by a comparison of the carrying amount of assets to future undiscounted net cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amounts of the assets exceed the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less cost to sell. The Company tests impairment of long-lived assets and intangible assets at the reporting unit level when impairment indicator appeared and recognizes impairment in the event that the carrying value exceeds the fair value of each reporting unit. The impairment charges for intangible assets for the years ended December 31, 2011, 2012 and 2013 were \$1.3 million, \$8.6 million, and \$3.6 million, respectively.

#### ***m. Receipts in advance and deferred revenues***

For the Company's online games business, proceeds received from sales of prepaid game cards form the basis of the revenues and are initially recorded as receipts in advance from players and are transferred from receipts in advance to deferred revenues when the prepaid cards are activated or charged by the players to their respective personal game accounts. For games that the Company licenses to third-party operators, deferred revenues represent the unamortized balance of initial license fees paid by overseas licensees.

Deferred revenues from Web game operations mainly represent the unamortized balance of initial license fees paid by third-party joint operators of the Company's Web games and unrecognized revenue-sharing related to virtual items that are not consumed. In cases where the joint operation agreement with joint operator requires the Company to set up and maintain the servers to host the Web games for the users, the Company is obliged to provide on-going services to users and the Company recognizes revenue when virtual items are consumed. For a discussion of revenue recognition with respect to the Company's Web game operations, see "Web games" in Note 4(s).

For the online advertising business, cash payments, which are received in advance of the delivery of online advertising services pursuant to applicable advertising contracts, are recorded as receipts in advance.

#### ***n. Contingent Consideration***

The acquisition of 7Road includes a contingent consideration arrangement that requires additional consideration to be paid by the Group based on the future financial performance of 7Road through December 31, 2012. The range of the undiscounted amounts the Company could pay under the contingent consideration agreement is between \$nil and \$32.76 million. The fair value of the contingent consideration of \$28.05 million recognized on the acquisition date was estimated by an independent valuation firm, with the income approach applied. There were no indemnification assets involved. As of the end of 2012, 7Road had exceeded the financial performance milestones and as a result changes in the fair value of the contingent consideration of \$2.2 million were recognized in other expense for the year ended December 31, 2012.



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The acquisition of Doyo includes a contingent consideration arrangement that requires additional consideration to be paid by the Group based on the future financial performance of Doyo for the fiscal years 2013 through 2015. The range of the undiscounted amounts the Group could pay under the contingent consideration agreement is between \$nil and \$7.3 million. The fair value of the contingent consideration, in the amount of \$4.8 million, was recognized on the acquisition date using the income approach/discounted cash flow method with a scenario analysis applied. There were no indemnification assets involved. As of the end of 2013 Doyo had exceeded the financial performance milestones for 2013 and as a result changes in the fair value of the contingent consideration of \$0.1 million were recognized in other expenses for the year ended December 31, 2013.

The acquisition of the RaidCall Business includes a contingent consideration arrangement that gives the Group the right to acquire additional shares of TalkTalk if specified conditions occur through the 2014 fiscal year. The range of the additional shares of TalkTalk that the Group could acquire under the contingent consideration agreement is between nil and 7.5% of the outstanding shares on a post-issuance, fully-diluted basis. The fair value of the contingent consideration of \$nil was recognized on the acquisition date, as management determined that it is unlikely that the specified conditions will occur and that as a result the fair value and the financial impact on recognition of the non-controlling interest was zero.

#### *o. Mezzanine Equity*

Mezzanine Equity consists of non-controlling interest in 7Road and a put option pursuant to which the non-controlling shareholders will have the right to put their equity interests in 7Road to the Company at a pre-determined price if 7Road achieves specified performance milestones before the expiry of the put option and 7Road does not complete an initial public offering on NASDAQ, the New York Stock Exchange or The Stock Exchange of Hong Kong. The put option will expire in 2014. Since the occurrence of the put is not solely within the control of the Company, the Company classifies the non-controlling interest as mezzanine equity instead of permanent equity in the Company's consolidated financial statements.

In accordance with ASC subtopic 480-10, the Company calculates, on an accumulative basis from the acquisition date, (i) the amount of accretion that would increase the balance of non-controlling interest to its estimated redemption value over the period from the date of the 7Road acquisition to the earliest redemption date of the non-controlling interest and (ii) the amount of net profit attributable to non-controlling shareholders of 7Road based on their ownership percentage. The carrying value of the non-controlling interest as mezzanine equity will be adjusted by an accumulative amount equal to the higher of (i) and (ii). See Note 19 – "MEZZANINE EQUITY."

On May 1, 2013, Changyou entered into an agreement to acquire all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders and all of the equity interests in Shenzhen 7Road held by shareholders other than Gamease. The acquisition closed on June 5, 2013. Under ASC 810-10, changes in a parent's ownership interest while the parent retains control of its subsidiary are accounted for as equity transactions, and do not impact net income or comprehensive income in the consolidated financial statements. Following the closing of the acquisition, \$2.4 million, representing the excess of the amount of the mezzanine-classified non-controlling interest in 7Road Cayman over the purchase price as of the closing date, was recorded in the Group's equity accounts.

#### *p. Non-controlling interest*

Non-controlling interests are recognized to reflect the portion of the equity of majority-owned subsidiaries and VIEs which is not attributable, directly or indirectly, to the controlling shareholder. Currently, the non-controlling interests in the Company's consolidated financial statements primarily consist of non-controlling interests for TalkTalk.

#### *q. Treasury Shares*

On July 27, 2013, the Company's Board of Directors authorized a share repurchase program of up to \$100 million of the outstanding ADSs of Changyou over a two-year period from July 27, 2013 to July 26, 2015. The Company accounted for those shares repurchased as treasury shares at cost in accordance with ASC 505-30, and the treasury shares acquired are shown separately in the shareholders' equity as the Company has not yet decided on the ultimate disposition of those shares. If and when the Company cancels the treasury shares, the difference between the original issuance price and the repurchase price will be debited into additional paid-in capital. See Note 25 – "TREASURY SHARES".



***r. Foreign currency translation***

The Company's functional and reporting currency is the United States dollar ("U.S. dollar"). The functional currency of the Company's subsidiaries and VIEs in China is the Renminbi ("RMB"). The functional currency of the Company's subsidiary in the United Kingdom is the British Pound, the functional currency of the Company's subsidiary in Malaysia is the Malaysian Ringgit, the functional currency of the Company's subsidiary in Korea is the South Korean Won, the functional currency of the Company's subsidiaries in the British Virgin Islands, Hong Kong and the United States of America is the U.S. dollar. Accordingly, assets and liabilities of the China subsidiaries and VIEs are translated at the current exchange rate in effect at the balance sheet date, and revenues and expenses are translated at the average exchange rates for RMB to U.S. dollars in effect during the reporting period. Gains and losses resulting from foreign currency translation to reporting currency are recorded in accumulated other comprehensive income in the consolidated statements of shareholders' equity for the years presented.

Foreign currency transactions are translated at the applicable rates quoted by the People's Bank of China ("PBOC") prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are re-measured at the applicable rates of exchange in effect at that date. Gains and losses resulting from foreign currency re-measurement are included in the consolidated statements of comprehensive income.

***s. Revenue recognition***

**Online Game Revenues**

***MMOGs***

The Group earns revenue through providing MMOGs to players pursuant to the item-based revenue model. Under the item-based model, the basic game play functions are free of charge and players are charged for purchases of in-game virtual items.

Game operations revenues are collected by the Company's VIEs through the sale of the Group's prepaid cards, which the Group sells in both virtual and physical forms to third-party distributors and players. Proceeds received from sales of prepaid cards are initially recorded as receipts in advance from customers and, upon activation or charge of the prepaid cards, are transferred from receipts in advance from customers to deferred revenues. As the Group does not have control of, and generally does not know, the ultimate selling price of the prepaid cards sold by distributors, net proceeds from distributors form the basis of revenue recognition.

Under the item-based revenue model, revenue is recognized over the estimated lives of the virtual items purchased or as the virtual items are consumed. If different assumptions were used in deriving the estimated lives of the virtual items, the timing in which the Group records its revenues would be impacted.

Revenues are recorded net of business tax, discounts and rebates to distributors.

Prepaid cards will expire two years after the date of card production if they have never been activated. The proceeds from the expired game cards are recognized as revenue upon expiration of cards.

Once the prepaid cards are activated and credited to a player's personal game account, they will not expire as long as the personal game account remains active. The Group is entitled to suspend and close a player's personal game account if it has been inactive for a period of 180 consecutive days. The unused balances in an inactive player's personal game account are recognized as revenues when the account is suspended and closed.

For the years ended December 2011, 2012 and 2013, the Group recognized revenues in connection with expired un-activated prepaid cards and unused balances in inactive accounts of approximately \$964,000, \$627,000, and \$951,000 respectively.

***Web games***

The Group began generating Web game revenues upon its acquisition of a controlling interest in 7Road in May 2011.



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Revenues from Web games were derived mainly from revenue-sharing payments from third-party joint operators of the Group's games and license fees from certain of these joint operators. The Group also derives revenues from direct operation of Wartune and DDTank on its own Websites for the games. Web games are operated primarily under the item-based revenue model, in which game players can access the games free of charge, but may purchase consumable virtual items, including those with a predetermined expiration time, or perpetual virtual items, such as certain costumes that stay bound to a game player throughout the life of the game. In certain of the joint operation arrangements for Web games, the Group provides the games and related services to a third-party joint operator at no upfront fee. In these arrangements, the Group is entitled to a single stream of revenue-sharing payments from the joint operator when game players convert the joint operator's virtual currency into game coins or purchase the Group's game coins directly through such operator's Website or game platform. Certain of the joint operators pay the Group license fees for the exclusive right to operate its games in specified geographic areas or upon achievement of certain performance milestones from the joint operators' operation of the games. Certain of the joint operators also pay the Group license fees for the right to be among a selected few who will have the initial right ahead of other operators to jointly operate the games in China during a specified period after their launch.

When the Group's Web games are jointly operated through the Websites or platforms of third-party joint operators, the Group views the third-party joint operators as its customers and recognizes revenues on a net basis as the Group does not have the primary responsibility for fulfillment and acceptability of the game services. The games may be hosted either on the third-party operators' servers or on servers that the Group owns or leases from Internet data centers. For arrangements where the game is hosted on the joint operators' servers, the game is delivered to the joint operators at the commencement of the joint operation period. The amount of revenue is recognized at the time of conversion, using a usage-based model under ASC 985-605, "*Software—Revenue Recognition*" and is measured based on the portion to which the Group is entitled of the amount of game players' purchase of the Group's game coins through the joint operators' Websites or game platforms. For arrangements where the game is hosted on the Group's servers, the Group accounts for multiple elements under ASC 605-25, "*Revenue Recognition—Multiple Element Arrangements*," as the joint operators have the right to obtain the games' software without penalty, and it is technically feasible for them to host the software. There are two separate units of accounting identified as (i) the game and related service elements and (ii) the hosting service element. The game and related service elements are accounted for under ASC 985-605 and for the hosting services which are accounted for under ASC 605, revenue is recognized over the implicit service period during which the Group is obligated to provide access to the server for the game players of the joint operators' platforms to be able to consume virtual items.

For the Group's direct operation of its Web games Wartune and DDTank through its Website for the game, the Group recognizes revenues on a gross basis as the Group has the primary responsibility for fulfillment and acceptability of the game services. The Group is obligated to provide on-going services to the game players, and such obligation is not deemed to be inconsequential and perfunctory after game players purchase its game coins directly through its Website for Wartune and DDTank. Therefore, the Group's revenues from direct operation of Wartune and DDTank on its Website for the game are first recorded as deferred revenues and subsequently recognized as revenue over the service period during which the Group is obligated to provide services to the game players to enable them to consume their virtual items.

License revenues from operators who have been granted the exclusive right to operate the Group's games in specified geographic areas where the Group does not provide hosting services are accounted for under ASC 985-605, "*Software—Revenue Recognition*." Since the Group is required to provide when-and-if-available updates and upgrades to the Joint Operators during the contract terms for which the Group does not have vendor-specific objective evidence of fair value, such license fees are initially recorded as deferred revenues and then recognized as revenues ratably over the contract periods from the date the game is launched, or in the case of license fees contingent upon achievement of performance milestones, over the remaining contract periods commencing from the date on which such milestones are achieved. License revenues from operators who have been granted the right to be among a selected few who will have the initial right ahead of other operators to jointly operate the Group's games in China during a specified period after their launch are recognized ratably over the specified exclusive operation period.

Most of the Group's revenues from the joint operation of its Web games within China, which are generated through Shenzhen 7Road, are subject to 17% PRC VAT, and Shenzhen 7Road, as a "software enterprise," is entitled to a 14% VAT refund immediately upon the filing of its VAT returns, with the result that Shenzhen 7Road's net effective PRC VAT rate is 3%. The amount of PRC VAT included in the Group's revenues for the year ended December 31, 2013 was \$9.3 million, compared to \$8.8 million and \$1.9 million, respectively, for the year ended December 31, 2012 and 2011.





### *Games licensed to third-party operators*

The Group enters into licensing arrangements with third-party operators to operate the Group's MMOGs in other countries or regions. These licensing agreements provide two revenue streams, consisting of an initial license fee and a monthly revenue-based royalty fee based on monthly revenue and sales from ancillary products of the games. The initial license fee is based on both a fixed amount and additional amounts receivable upon the game's achieving certain sales targets. Since the Group is obligated to provide post-sales services such as technical support and provision of updates and when-and-if-available upgrades to the licensees during the license period, the initial license fee from the licensing arrangement is recognized as revenue ratably over the license period. The fixed amount of the initial license fee is recognized ratably over the remaining license period from the launch of the game and the additional amount is recognized ratably over the remaining license period from the date such additional amount is certain. The monthly revenue-based royalty fee is recognized when relevant services are delivered, provided that collectability is reasonably assured.

### *Online Advertising Revenues*

The Group's online advertising revenues are generated from the 17173 Business. A contract is signed to establish a fixed price and the advertising services to be provided. Based on the contracts, the 17173 Business provides advertisement placements on its Websites and/or in different formats, including, among other things, banners, links, logos, buttons, rich media and content integration.

To determine the method of recognition of online advertising revenue, prior to entering into contracts, management makes a credit assessment of the customer to assess the collectability of the contract. For those contracts for which collectability is determined to be reasonably assured, revenue is recognized ratably over the period during which the advertising services are provided and when all revenue recognition criteria are met. For those contracts for which collectability is determined to not be reasonably assured, revenue is recognized only when the cash is received and all other revenue recognition criteria are met.

Before 2011, the 17173 Business treated multiple deliverable elements of advertising contracts as a single unit of accounting for revenue recognition purposes. On January 1, 2011, in accordance with ASU No.2009 -13, the 17173 Business began to treat advertising contracts with multiple deliverable elements as separate units of accounting for revenue recognition purposes and to recognize revenue on a periodic basis during the contract periods when each deliverable service was provided. Since the contract price is for all the deliverables under an advertising contract, the 17173 Business allocates the contract price among all the deliverables at the inception of the arrangement on the basis of their relative selling prices according to the selling price hierarchy established by ASU No.2009 -13. The 17173 Business first uses vendor-specific objective evidence of selling price, if it exists. If vendor-specific objective evidence of selling price does not exist, the 17173 Business uses third-party evidence of selling price. If neither vendor-specific objective evidence of selling price nor third-party evidence of selling price exists, the 17173 Business uses management's best estimate of the selling price for the deliverable.

A pilot program for transition from the imposition of Business Tax to the imposition of VAT for revenues from certain industries (the "Pilot Program") was launched in Shanghai on January 1, 2012. Effective September 1, 2012, the Pilot Program was expanded from Shanghai to eight other cities and provinces in China, including Beijing. Online advertising revenues became subject to VAT on September 1, 2012, at a rate of 6%. Online advertising revenues are recognized after deducting agent rebates and net of VAT and related surcharges.

### *IVAS Revenues*

The Group offers Web games developed by third-party developers and generate revenues from the provision of IVAS, including promotion, access maintenance and payment services, to third-party developers. Under revenue-sharing agreements that the Group signs with third-party developers, the Group collects payments from the end users, keeps a pre-agreed percentage of the proceeds and remits the balance to the third-party developers. Revenues from IVAS are recognized when the Group's obligations under the agreements and all other revenue recognition criteria have been met. Revenues from IVAS are recognized using the gross method as the Group is the principal obligor with respect to provision of the services.

### *Others Revenues*

For cinema advertising revenues, a contract is signed with the advertiser to establish a fixed price and specify advertising services to be provided. Based on the contracts, the Group provides advertisement placements in advertising slots to be shown in theatres before the screening of movies. Revenue from cinema advertising is recognized when all the recognition criteria are met. Depending on the terms of a customer contract, fees for services performed can be recognized according to two principal methods, consisting of the proportional performance method and the straight-line method. Under the proportional performance method, fees are generally recognized based on a percentage of the advertising slots actually delivered where the fee is earned on a per-advertising slot placement basis. Under the straight-line method, fees are recognized on a straight-line basis over the contract period when the fee is not paid based on the number of advertising slots actually delivered.



## Presentation of PRC Value Added Tax and Business Tax

Under ASC 605-45, the presentation of taxes on either a gross basis (included in revenues and costs) or a net basis (excluded from revenues) is an accounting policy decision determined by management.

As VAT imposed on online advertising and cinema advertising revenues and VAT imposed on 7Road's revenues deemed to be from the sale of software are considered as substantially different in nature, the Group determined that it is reasonable to apply the guidance separately for these two types of VAT. VAT payable on online advertising and cinema advertising revenues is the difference between the output VAT (at a rate of 6%) and available input VAT amount (at the rate applicable to the supplier) which is the VAT paid to suppliers in relation to the cost for provision of online advertising and cinema advertising services. On the other hand, VAT is payable by 7Road at an effect effective rate of 3% of revenues deemed to be from the sale of software, irrespective of the availability of any input VAT, under preferential VAT treatment provided to 7Road by the local tax bureau.

The Group adopted the net presentation method for its MMOG revenues, online advertising revenues and cinema advertising revenues and adopted the gross presentation method for the revenues of 7Road deemed to be derived from the sale of software. Under net presentation methods, revenues are net of business tax (at a rate of 5%) or value added tax (at a rate of 6%).

Under gross presentation methods, the Company presents PRC VAT on a gross basis, by which VAT collected from customers at the rate of 17% is included in revenues, and the net VAT payment at the effective PRC VAT rate of 3% is included in cost of revenues, because the Company considers 7Road's 17% VAT obligation and its entitlement to a 14% VAT refund as one integrated preferential VAT policy.

### *t. Cost of revenues*

Cost of online game revenues mainly consists of salary and benefits, revenue-based royalty payments to the game developers, bandwidth leasing charges, amortization of licensing fees, depreciation expenses, business tax and value-added tax which primarily arise from the revenue that AmazGame and Gamespace derive from their contractual arrangements with Gamease and Guanyou Gamespace, respectively, and other direct costs.

Cost of online advertising revenues mainly consists of salary and benefit, bandwidth leasing costs, depreciation expenses, and advertising design cost.

Cost of IVAS mainly consists of revenue-sharing arrangements with developers.

Other cost of revenues mainly consists of payments to theatres and film production companies for pre-film screening advertising slots and charges for impairment of intangible assets.

### *u. Product development expenses*

Costs incurred for the development of online games and the 17173.com Website and other platform channels prior to the establishment of technological feasibility and costs incurred for maintenance after the online games and platform channels are available for marketing are expensed when incurred and are included in product development expenses.

During the years ended December 31, 2011, 2012 and 2013, the Company did not capitalize any product development expense.

### *v. Government Grant*

A government grant is recognized when the grant is received and the relevant requirements have been complied with. Government grants are generally recorded as other income, and grants for which the government stipulates specified uses are recorded as a reduction in operating expenses and cost of revenues. For the years ended December 31, 2011, 2012 and 2013, awards from the PRC government recorded in other income were \$16,000, \$3,422,000 and \$2,632,000, respectively, awards recorded as a reduction in operating expenses were \$126,000, \$158,000 and \$398,000 respectively, and awards recorded as a reduction in cost of revenues were \$nil, \$nil, and \$507,000, respectively.

### *w. Advertising expense*

Advertising expenses, which generally represent the cost of promotions to create or stimulate a positive image of the Company or a desire to buy the Company's products and services, are expensed as incurred. Included in sales and marketing expense are advertising costs of \$33.4 million, \$42.3 million and \$101.6 million, respectively, for the years ended December 31, 2011, 2012 and 2013. Advertising expenses charged from Sohu were \$6.0 million, \$14.0 million and \$13.4 million, respectively, for the years ended December 31, 2011, 2012 and 2013.



#### *x. Operating leases*

Leases for which substantially all of the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received by the Company from the leasing company are charged to the consolidated statements of comprehensive income on a straight-line basis over the lease periods.

#### *y. Share-based compensation expense*

Share-based compensation expense is for share awards, including ordinary shares, share options, restricted shares and restricted share units, granted by the Company to employees and directors. Share-based compensation expense of employees is recognized as costs and/or expenses in the financial statements based on the fair values of the related share-based awards on their grant dates.

Changyou has an incentive plan for the granting of share-based awards, including share options, restricted shares and restricted share units, to their employees and directors. 7Road's 2012 Share Incentive Plan was cancelled effective June 28, 2013. See Note 18 "SHARE-BASED COMPENSATION—Share Awards Granted after Initial Public Offering—7Road 2012 Share Incentive Plan."

For share-based awards, in determining the fair value of ordinary shares, restricted shares and restricted share units granted before the shares underlying the awards were publicly traded, the income approach/discounted cash flow method with a discount for lack of marketability was applied. In determining the fair value of restricted share units granted shortly before Changyou's initial public offering, the fair value of the underlying shares was determined based on the offering price in the initial public offering. In determining the fair value of restricted share units granted after Changyou's initial public offering, the public market price of the underlying shares on the grant dates is applied. In determining the fair value of share options granted by Sohu to employees of Changyou prior to its initial public offering, the Company applied the Black-Scholes valuation model.

Determining the fair value of the ordinary shares not publicly traded required complex and subjective judgments regarding the Company's projected financial and operating results, its unique business risks, the liquidity of its ordinary shares and its operating history and prospects at the time the grants were made. The assumptions used in share-based compensation expense recognition represent management's best estimates based on historical experience and consideration to developing expectations about the future. However, these estimates involve inherent uncertainties and the application of management judgment. If factors change or different assumptions are used, the share-based compensation expense could be materially different for any period. Moreover, the estimates of fair value are not intended to predict actual future events or the value that ultimately will be realized by employees who receive equity awards, and subsequent events are not indicative of the reasonableness of the original estimates of fair value made by the Company for accounting purposes.

Share-based compensation expense for share options, restricted shares and restricted share units granted is recognized on an accelerated basis over the requisite service period. The number of share-based awards for which the service is not expected to be rendered over the requisite period is estimated, and the related compensation expense is not recorded for that number of awards.

#### *z. Income taxes*

Current income taxes are provided on the basis of income for financial reporting purposes, adjusted for income and expense items which are not assessable or deductible for income tax purposes, in accordance with the regulations of the relevant tax jurisdictions. Deferred income taxes are provided using the liability method. Under this method, deferred income taxes are determined based on the differences between the financial reporting and tax bases of assets and liabilities and are measured using the currently enacted tax rates and laws. The deferred tax assets are reduced by a valuation allowance if it is considered based on available evidence more likely than not that some portion, or all, of the deferred tax assets will not be realized. Deferred tax liability is not recognized for undistributed earnings of PRC subsidiaries if the subsidiary has invested or will invest the undistributed earnings indefinitely.

#### *aa. Uncertain tax positions*

In order to assess uncertain tax positions, the Company applies a more likely than not threshold and a two-step approach for the tax position measurement and financial statement recognition. For the two-step approach, the first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon settlement.



***ab. Earnings per share***

Basic earnings per share is computed using the weighted average number of ordinary shares outstanding during the year. Diluted earnings per share is computed using the weighted average number of ordinary shares and, if dilutive, potential ordinary shares outstanding during the year. Potential ordinary shares consist of shares issuable upon the exercise of stock options and shares issuable upon the settlement of restricted share units. Potential ordinary shares are accounted for in the computation of diluted earnings per share using the treasury share method. Potential ordinary shares are not included in the denominator of the diluted earnings per share calculation when inclusion of such shares would be anti-dilutive, such as in a period in which a net loss is recorded. Earnings per share is computed on Class A ordinary shares and Class B ordinary shares together, because both classes have the same dividend rights and the same participation rights in the Company's undistributed earnings.

***ac. Comprehensive income***

Comprehensive income is defined as the change in equity of a company during a period from transactions and other events and circumstances excluding transactions resulting from investments from owners and distributions to owners. Accumulated other comprehensive income, as presented on the accompanying consolidated balance sheets, consists of the cumulative foreign currency translation adjustment.

***ad. Segment reporting***

Operating segments are defined as components of an enterprise about which separate financial information is available and is evaluated regularly by the chief operating decision maker ("CODM"), or a decision making group, in deciding how to allocate resources and in assessing performance. The Company's CODM is its Chief Executive Officer.

The Company's organizational structure is based on a number of factors that the CODM uses to evaluate, view and run the Company's business operations, which include, but are not limited to, customer base, homogeneity of products and technology. The Company's operating segments are based on its organizational structure and information reviewed by the Company's CODM to evaluate the operating segment results.

The Company has determined that the business segments that constitute its primary reportable segments are the online game segment, which consists of MMOGs and Web games, and the 17173 Business segment, which consists of the online advertising business and the IVAS business.

Before 2011, the Group principally engaged in the development, operation and licensing of MMOGs and operated and managed this business as a single segment. In 2011, Changyou expanded its business by acquisitions in the Web game, online advertising and cinema advertising businesses, and generated revenues from the operations of such businesses. With the goal of optimizing the management of operations, the Company's CODM separately reviewed key information of each of four operating segments consisting of MMOG, Web game, the 17173 Business and cinema advertising. The Company concluded that the MMOG and Web game have similar economic characteristics and meet all of the aggregation criteria that are required under ASC280 to aggregate identified operating segments. Hence the Company aggregated MMOG and Web game as one reportable segment under online game. In addition, cinema advertising is not deemed significant enough to qualify as a separate, reportable segment and therefore is included in the "others."

***ae. Recently issued accounting standards***

In March of 2013, the FASB issued guidance on "Foreign Currency Matters, Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity." The amendments clarify the applicable guidance for the de-recognition of all or a portion of a cumulative translation adjustment when an entity ceases to have a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business (other than a sale of in substance real estate or conveyance of oil and gas mineral rights) within a foreign entity or when other changes stipulated occur and involve a foreign entity. The amendments are effective prospectively for fiscal years (and interim reporting periods within those years) beginning after December 15, 2013. The Group is currently evaluating the impact on its consolidated financial statements of adopting this guidance.



In March of 2013, the FASB issued guidance on “Income Taxes - Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists.” The amendments clarify that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss, similar tax loss, or tax credit carryforward, except as noted in the following sentence. To the extent a net operating loss, similar tax loss, or tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such a purpose, then under this exception the unrecognized tax benefit is to be presented in the financial statements as a liability and should not be combined with (netted with) the deferred tax asset(s). The assessment of whether a deferred tax asset is “available” is based on the unrecognized tax benefit and deferred tax asset amounts that exist at the reporting date and should be made presuming disallowance of the tax position at the reporting date. The amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. The Group is currently evaluating the impact on its consolidated financial statements of adopting this guidance.

## 5. CONCENTRATION OF RISKS

There are no revenues from distributors that individually represent exceeding 10% of the total revenues for the years ended December 31, 2011, 2012 or 2013.

Approximately 74%, 68% and 64%, respectively, of the Group’s net revenues for the year ended December 31, 2011, 2012 and 2013 were derived from a single MMORPG, Tian Long Ba Bu, which was launched in May 2007.

Approximately 96%, 95% and 91%, respectively, of the Group’s net revenues for the years ended December 31, 2011, 2012 and 2013 were derived from domestic operations.

Substantially all the Company’s long-lived assets are located in the PRC.

A majority of the Group’s sales and expenses transactions are denominated in RMB and a significant portion of the Group’s assets and liabilities is denominated in RMB. The RMB is not freely convertible into foreign currencies. In the PRC, certain foreign exchange transactions are required by law to be transacted only by authorized financial institutions at exchange rates set by the PBOC. Remittances in currencies other than RMB by the Group in China must be processed through the PBOC or other China foreign exchange regulatory bodies, which require certain supporting documentation in order to affect the remittance. Total cash and cash equivalents in currencies other than RMB held at financial institutions in mainland China were \$2.2 million and \$4,000, respectively, as of December 31, 2012 and 2013.

The Group holds its cash and bank deposits at Chinese financial institutions that are among the largest and most respected in the PRC and at international financial institutions with high ratings from internationally-recognized rating agencies. The Company’s management chooses these institutions because of their reputations and track records for stability, and their known large cash reserves, and management periodically reviews these institutions’ reputations, track records, and reported reserves. Management expects that any additional institutions that the Group uses for its cash and bank deposits will be chosen with similar criteria for soundness. As a further means of managing its credit risk, the Group held its cash and bank deposits in approximately 21 and 22 different financial institutions as of December 31, 2012 and 2013, respectively, and held no more than approximately 36% and 32%, of its total cash at any single institution as of December 31, 2012 and 2013, respectively.

Under PRC law, it is generally required that a commercial bank in the PRC that holds third party cash deposits protect the depositors’ rights over and interests in their deposited money; PRC banks are subject to a series of risk control regulatory standards; and PRC bank regulatory authorities are empowered to take over the operation and management of any PRC bank that faces a material credit crisis.



**6. BUSINESS COMBINATIONS***Acquisition of Shanghai Jingmao and its affiliate*

In May 2010, in order to diversify the Group's marketing channels for its games, the Group acquired 50% of the equity interests in each of Shanghai Jingmao and its affiliate, which are primarily engaged in the cinema advertising business in China. The investment was accounted for under the equity method of accounting due to the group's inability to control Shanghai Jingmao. In January 2011, the Group acquired the remaining 50% of the equity interests in each of Shanghai Jingmao and its affiliate for total consideration of approximately \$3.0 million. Payments for \$1.0 million of the total consideration are contingent upon occurrence of certain specified events and management considers the possibility of the Group making gains due to the non-occurrence of the specified events to be remote. With unilateral control of 100% of the voting equity interests of Shanghai Jingmao and its affiliate, the Company started to consolidate Shanghai Jingmao and its affiliate's financial statements on February 1, 2011. On the acquisition date, the allocation of the consideration of the assets acquired and liabilities assumed based on their fair values was as follows:

	As of February 1, 2011 (in thousands)
Fair value of previously held 50% equity interests	\$ 2,704
Consideration for the remaining 50% equity interests	3,036
Total consideration	5,740
Tangible assets	9,514
Identifiable intangible assets acquired	10,101
Goodwill	5,147
Liabilities assumed	(19,022)
Total	\$ 5,740

In accordance with ASC805 in a business combination achieved in stages, the Group re-measured its previously held equity interests in Shanghai Jingmao and its affiliate as at their acquisition-date fair value using the discounted cash flow method and recognized a total loss of \$613,000 in other expenses in the first quarter of 2011. The Group hired an independent valuation firm to perform fair valuation of the previously held equity interests in Shanghai Jingmao and its affiliate upon the acquisition date.

The excess of the purchase price over tangible assets, identifiable intangible assets acquired, and liabilities assumed was recorded as goodwill relating to the others business segment. The acquired identifiable intangible assets were valued by various approaches, including the income approach and the replacement cost approach, as appropriate. As of December 31, 2013, no measurement period adjustment had been recorded.

Prior to the acquisition, Shanghai Jingmao and its affiliate did not prepare financial statements in accordance with U.S. GAAP. The Company determined that the cost of reconstructing the financial statements of Shanghai Jingmao and its affiliate for the periods prior to the acquisition outweighed the benefits. Based on an assessment of the financial performance of all companies acquired by the Group and a comparison of Shanghai Jingmao and its affiliate's and the Group's financial performance for the fiscal year prior to the acquisition, the Company did not consider Shanghai Jingmao and its affiliate on their own to be material to the Group. Thus the Company's management believes the presentation of pro forma financial information with respect to the results of operations of the Group for the business combination is not necessary.

Total identifiable intangible assets acquired upon acquisition mainly include cinema advertising slot rights of \$8,330,000, partnership relationship of \$1,035,000, trade name of \$502,000, non-compete agreement of \$126,000, and customer list of \$108,000. Except for trade name, which is expected to have an indefinite useful life, other identifiable intangible assets acquired have an estimated average weighted useful life of two years. Under ASC350, intangible assets with an indefinite useful life are not amortized and their remaining useful life is evaluated at each reporting period to determine whether events and circumstances continue to support an indefinite life. Charges for acquired intangible assets for the years ended December 31, 2011, 2012 and 2013 were \$0.2 million, \$1.2 million, and \$nil respectively. Goodwill primarily represents the expected synergies from combining operations of Shanghai Jingmao and its affiliate with those of the Group, which are complementary to each other. In accordance with ASC350, goodwill is not amortized but is tested for impairment and is not deductible for tax purposes. For the year ended December 31, 2011, a full impairment loss of \$5.2 million on Shanghai Jingmao's goodwill was recognized.

**Acquisition of 7Road**

On May 11, 2011, the Group acquired 68.258% of the equity interests of Shenzhen 7Road for fixed cash consideration of approximately \$68.26 million, plus additional variable cash consideration of up to a maximum of \$32.76 million that is contingent upon the achievement of specified performance milestones through December 31, 2012. Shenzhen 7Road is primarily engaged in Web game operations, through third party joint operators, and development. The Company began to consolidate Shenzhen 7Road's financial statements on June 1, 2011. The purpose of the acquisition was to accelerate the Group's position in China's online games industry and add a new category of games to the Group's growing product portfolio. On the acquisition date, the allocation of the consideration of the assets acquired and liabilities assumed based on their fair value was as follows:

	As of June 1, 2011 (in thousands)
Cash consideration	\$ 68,258
Contingent consideration	28,051
Total consideration	96,309
Receivables	7,440
Other tangible assets	22,213
Completed game	20,837
Games under development	3,561
Other identifiable intangible assets acquired	986
Goodwill	103,366
Liabilities assumed	(8,983)
Fair value of non-controlling interest and put option	(53,111)
Total	\$ 96,309

The excess of the purchase price over tangible assets, identifiable intangible assets acquired, and liabilities assumed was recorded as goodwill relating to the online game segment. Charges for impairment of acquired intangible assets for the years ended December 31, 2011, 2012 and 2013 were \$nil, \$0.6 million and \$nil, respectively. The acquired identifiable intangible assets were valued by various approaches, including the income approach and the replacement cost approach, as appropriate. As of December 31, 2013, no measurement period adjustment had been recorded.

Prior to the acquisition, Shenzhen 7Road did not prepare its financial statements in accordance with U.S. GAAP. The Company determined that the cost of reconstructing the financial statements of Shenzhen 7Road for the periods prior to the acquisition outweighed the benefits. Based on an assessment of the financial performance of all companies acquired by the Group and a comparison of Shenzhen 7Road's and the Group's financial performance for the fiscal year prior to the acquisition, the Company did not consider Shenzhen 7Road on its own to be material to the Group. Thus the Company's management believes the presentation of pro forma financial information with respect to the results of operations of the Group for the business combination is not necessary.

The fair value of non-controlling interest in Shenzhen 7Road was determined mainly based on the number of shares held by non-controlling shareholders and the equity value close to the acquisition date, taking into consideration other factors, as appropriate. If Shenzhen 7Road achieved specified performance milestones and 7Road (after the 7Road Reorganization) did not complete an initial public offering on NASDAQ, the New York Stock Exchange or The Stock Exchange of Hong Kong, the non-controlling shareholders had the right to put their equity interests in 7Road to the Group at a predetermined price agreed upon at the acquisition date ("the put option"). In accordance with ASC480, the Company measured this non-controlling interest and a put option at their acquisition-date fair value. An independent valuation firm was hired to determine the fair value upon the acquisition date.

The agreement for the acquisition of Shenzhen 7Road included a contingent consideration arrangement that required additional consideration to be paid by the Group based on the financial performance of Shenzhen 7Road over a period through December 31, 2012. The range of the undiscounted amounts the Company could have paid under the contingent consideration provisions of the agreement was between \$nil and \$32.76 million. The fair value of the contingent consideration recognized on the acquisition date of \$28.05 million was estimated by an independent valuation firm, with the income approach applied. There were no indemnification assets involved. As of the end of 2012, 7Road had exceeded the financial performance milestones and as a result changes in fair value of the contingent consideration of \$2.2 million were recognized in other expense for the year ended December 31, 2012. Total identifiable intangible assets acquired upon acquisition mainly included completed game, games under development and other identifiable intangible assets acquired, including non-compete agreement of \$179,000, and relationship with operators of \$807,000. The games under development will be subject to amortization after completion. Completed game and other identifiable intangible assets acquired are amortized over an estimated average weighted useful life of five years. Total goodwill of \$103.4 million primarily represents the expected synergies from combining operations of Shenzhen 7Road with those of the Group, which were expected to be complementary to each other. In accordance with ASC350, goodwill is not amortized but is tested for impairment and is not deductible for tax purposes.

On May 1, 2013, Changyou entered into an agreement to acquire all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders, representing 28.074% of the outstanding share capital of 7Road, and all of the equity interests in Shenzhen 7Road held by shareholders other than Gamease, for aggregate cash consideration of approximately \$78 million. The acquisition closed on June 5, 2013. Effective with the closing, 7Road Cayman became an indirect wholly-owned subsidiary of Changyou, and Changyou's VIE Gamease became the sole shareholder of 7Road's VIE Shenzhen 7Road. As of December 31, 2013, Changyou had paid \$76 million of the total cash consideration. The remaining \$2 million will be settled in June 2014.

#### *Acquisition of the 17173 Business*

On December 15, 2011, the Group completed the acquisition from Sohu of certain assets and business operations associated with the 17173 Business for fixed cash consideration of approximately \$162.5 million. Under the acquisition agreement, the net profit of \$1.3 million generated from the Group's operation of the 17173 Business during the Transition Period from December 16, 2011 through December 31, 2011 was for the benefit of Sohu. The Company accounted for this \$1.3 million as part of the consideration for the acquisition. Since Changyou and the 17173 Business were controlled by Sohu both before and after the acquisition, this transaction was accounted for as a business combination under common control by Sohu. Therefore, in accordance with ASC subtopic 805-50, the consolidated financial statements of the Company include the acquired assets and liabilities of the 17173 Business at their historical carrying amounts of approximately \$22.0 million. In addition, the Group's consolidated financial statements as of and for the year ended December 31, 2011 were prepared as if the current corporate structure had been in existence.

The allocation of the consideration of the assets acquired and liabilities assumed based on their historical carrying amounts was as follows:

	As of December 31, 2011 (in thousands)
Cash consideration	\$ 162,500
Net profit for the Transition Period	1,284
Total consideration	163,784
Inventory	534
Fixed assets	2,737
Intangible assets	632
Goodwill	17,885
Deemed dividend to Sohu	141,996
Total	\$ 163,784

Changyou and Sohu separately entered into a services agreement and an online links and advertising agreement (collectively, the "Services and Advertising Agreements"), pursuant to which Sohu provide links and advertising space and technical support to the Company, including the provision and maintenance of user log-in, information management and virtual currency payment systems the 17173 Business. The Services and Advertising Agreements provide for a term of twenty-five years for the virtual currency payment system services, and an initial term of three years for all the other relevant services and links and advertising space, and involve aggregate fees to Sohu of approximately \$30 million. Under the Services and Advertising Agreements, the Company may renew certain rights for a subsequent term of twenty-two years, and may obtain a perpetual software license in respect of the information management system and the user log-in system following the expiration of the three-year term, subject to the Company's payment to Sohu of additional fees of up to approximately \$5 million in the aggregate.



### Acquisition of Doyo

In November 2013, the Group acquired 100% of the equity interests in Doyo, a game resources portal, for fixed cash consideration of approximately \$6.5 million, and variable cash consideration up to a maximum of \$7.3 million. Since Changyou has exclusive control of 100% of the voting equity interests of the Doyo, the Company began to consolidate Doyo's financial statements commencing with the acquisition. The Company views the acquisition of Doyo as an integral piece of the Company's strategy to enrich its application coverage in China.

The allocation of the consideration for assets acquired and liabilities assumed based on their historical carrying amounts was as follows:

	As of November 29, 2013 (in thousands)
Cash Consideration	\$ 6,521
Contingent Consideration	4,785
Total consideration	11,306
Tangible assets	1,324
Identifiable intangible assets acquired	3,620
Goodwill	7,626
Liabilities assumed	(1,264)
Total	\$ 11,306

Since Doyo is primarily engaged in online advertising and traffic monetization businesses, which have similar economic characteristics to the 17173 Business, Doyo is aggregated into the 17173 Business as a reporting unit and the excess of the purchase price over the tangible assets, identifiable intangible assets (mainly user base and domain names) acquired and liabilities assumed was recorded as goodwill relating to the 17173 Business. The acquired identifiable intangible assets were valued by various approaches, including the income approach, as appropriate. Total goodwill of \$7.6 million primarily represents the expected synergies from combining operations of the Company and Doyo, which are complementary to each other. In accordance with ASC350, goodwill is not amortized but is tested for impairment and is not deductible for tax purposes. As of December 31, 2013, no measurement period adjustment had been recorded.

Prior to the acquisition, Doyo did not prepare its financial statements in accordance with U.S. GAAP. The Group determined that the cost of reconstructing the financial statements of Doyo for the periods prior to the acquisition outweighed the benefits. Based on an assessment of the financial performance of all companies acquired by the Group and a comparison of Doyo's and the Group's financial performance for the fiscal year prior to the acquisition, the Group did not consider Doyo on its own to be material to the Group. Thus the Group's management believes the presentation of pro forma financial information with respect to the results of operations of the Group for the business combination is not necessary.

### Acquisition of the RaidCall Business

In December 2013, the Group acquired 62.5% of the equity interests, on a fully-diluted basis, in TalkTalk for cash consideration of \$47.6 million. Of the total consideration, \$27.6 million was paid by the Company to the Kalends Group for a portion of the ordinary shares of TalkTalk held by the Kalends Group, and \$20 million was injected for newly issued ordinary shares of TalkTalk. See Note 2.f "Acquisition of the RaidCall Business." On the acquisition date, the allocation of the consideration for assets acquired and liabilities assumed based on their fair values was as follows:

	As of December 24, 2013 (in thousands)
Cash Consideration	\$ 47,627
Tangible assets	20,016
Identifiable intangible assets acquired	17,888
Goodwill	33,740
Fair value of non-controlling interest	(17,172)
Liability assumed	(6,845)
Total	\$ 47,627

The excess of the purchase price over the tangible assets, identifiable intangible assets (consisting primarily of software technology and domain name) acquired and liabilities assumed was recorded as goodwill relating to the online game segment. Charges for impairment of acquired intangible assets for the year ended December 31, 2013 were \$nil. The acquired identifiable intangible assets were valued by the income approach. Total goodwill of \$33.7 million primarily represents synergies between the Company's existing online game business and the RaidCall Business that are expected to result from an enhancement of game players' experience through the Company's offering of the RaidCall communications tool with the Company's online games. In accordance with ASC350, goodwill is not amortized but is tested for impairment and is not deductible for tax purposes.

As of December 31, 2013, no measurement period adjustment had been recorded.

Prior to the acquisition, the RaidCall Business did not prepare its financial statements in accordance with U.S. GAAP. The Group determined that the cost of reconstructing the financial statements of the RaidCall Business for the periods prior to the acquisition outweighed the benefits. Based on an assessment of the financial performance of all companies acquired by the Group and a comparison of the Raidcall Business's and the Group's financial performance for the fiscal year prior to the acquisition, the Group did not consider the Raidcall Business on its own to be material to the Group. Thus the Group's management believes the presentation of pro forma financial information with respect to the results of operations of the Group for the business combination is not necessary.

## 7. BANK LOANS AND RESTRICTED TIME DEPOSITS

In 2012 and 2013, Changyou drew down loans from offshore branches of certain banks for the purposes of expediting the payment of a special one-time cash dividend to its shareholders, providing working capital to support its overseas operations, and funding the Company's acquisitions and the Company's share repurchase program. These bank loans were secured by an equivalent or greater amount of RMB deposits by Changyou in the onshore branches of such banks. The loans from the offshore branches of the lending banks are classified as short-term bank loans or long-term bank loans based on their payment terms.

As of December 31, 2013, the total amount of the bank loans was \$410.3 million, of which \$307.0 million carried a floating rate of interest based on the London Inter-Bank Offered Rate ("LIBOR") and \$103.3 million carried a fixed rate of interest. For the years ended December 31, 2012 and 2013, interest income from the restricted time deposits securing the loans was \$4.1 million and \$13.0 million, respectively, and interest expense on the bank loans was \$2.1 million and \$8.8 million, respectively.

## 8. ACCOUNTS RECEIVABLE, NET

The carrying amounts of accounts receivable of the Group are stated are as follows:

	As of December 31, (in thousands)	
	2012	2013
Accounts receivable	\$26,462	\$38,673
Less: provision for bad debts	(3,098)	(2,677)
<b>Net Book Value</b>	<b>\$23,364</b>	<b>\$35,996</b>

## 9. PREPAID AND OTHER CURRENT ASSETS

	As of December 31, (in thousands)	
	2012	2013
Refundable corporate income tax	\$ —	\$20,835
Accrued interest income	2,013	10,589
Prepayment for Sohu services	10,101	10,104
Rental deposits	2,307	4,305
Employee advance	1,252	3,430
Restricted cash	795	2,149
VAT refund receivables	2,355	2,118
Capitalized transaction cost	1,670	—
Deferred tax assets	2,229	4,743
Others	6,323	6,184
<b>Total</b>	<b>\$29,045</b>	<b>\$64,457</b>



**10. FIXED ASSETS, NET:**

	As of December 31, (in thousands)	
	2012	2013
Office building	\$ 36,261	\$207,987
Computer equipment (including servers)	52,349	56,852
Leasehold and building improvements	15,121	31,598
Office furniture	1,610	2,300
Vehicles	1,286	1,453
Total	106,627	300,190
Less: accumulated depreciation	(41,799)	(53,516)
<b>Net book value</b>	<b>\$ 64,828</b>	<b>\$246,674</b>

The depreciation expense for fixed assets was \$11.1 million, \$14.6 million and \$15.6 million, respectively, for the years ended December 31, 2011, 2012 and 2013. The balance of office building increased by \$171.7 million as the Company's headoffice in Beijing has been put into use in December 2013.

**11. INTANGIBLE ASSETS, NET**

The following table summarizes the Company's intangible assets, net:

Items	As of December 31, 2013 (in thousands)			
	Gross Carrying Amount	Accumulated Amortization	Impairment	Net Carrying Amount
Operating rights for licensed games	\$ 25,588	\$ (8,083)	\$ (7,244)	\$10,261
Computer software	5,379	(2,672)	(260)	2,447
Developed technologies	36,698	(12,870)	(3,432)	20,396
Trademarks and domain names	18,048	(3,939)	(543)	13,566
Cinema advertising slot rights	87,210	(61,314)	(4,115)	21,781
Others	7,406	(867)	(1,595)	4,944
<b>Total</b>	<b>\$180,329</b>	<b>\$ (89,745)</b>	<b>\$ (17,189)</b>	<b>\$73,395</b>

Items	As of December 31, 2012 (in thousands)			
	Gross Carrying Amount	Accumulated Amortization	Impairment	Net Carrying Amount
Operating rights for licensed games	\$ 14,092	\$ (4,871)	\$ (4,223)	\$ 4,998
Computer software	3,151	(1,589)	(260)	1,302
Developed technologies	27,289	(7,569)	(2,476)	17,244
Trademarks and domain names	9,215	(3,132)	(527)	5,556
Cinema advertising slot rights	71,064	(42,620)	(3,992)	24,452
Others	2,347	(714)	(936)	697
<b>Total</b>	<b>\$127,158</b>	<b>\$ (60,495)</b>	<b>\$ (12,414)</b>	<b>\$54,249</b>

The amortization expense for intangible assets was \$17.7 million, \$23.4 million and \$26.8 million, respectively, for the years ended December 31, 2011, 2012 and 2013.



As of December 31, 2013, amortization expense of intangible assets for future years is expected to be as follows:

	Amortization expense of intangible assets (in thousands)
2014	\$ 32,327
2015	17,592
2016	8,507
2017	2,483
2018	2,427
Thereafter	10,059
Total expected amortization expense	<u>\$ 73,395</u>

## 12. EQUITY INVESTMENTS

In January 2010, AmazGame acquired 30% of the equity interests in Shenzhen Zhou You Network Technology Ltd (“Zhou You”). Zhou You is primarily engaged in the online game development business.

In May 2010, AmazGame, through its wholly-owned subsidiary Yang Fan Jing He, acquired 50% of the equity interests of Shanghai Jingmao and its affiliate. Shanghai Jingmao and its affiliate are primarily engaged in the cinema advertising business. The Company had significant influence over Shanghai Jingmao and its affiliate. Therefore, the equity investments were accounted for using the equity method.

In January 2011, the Group acquired the remaining 50% of the equity interests in each of Shanghai Jingmao and its affiliate. With control of 100% of the voting equity interests of Shanghai Jingmao and its affiliate, the Company started to consolidate Shanghai Jingmao and its affiliate’s financial statements on February 1, 2011.

In August 2011, the Group acquired 10% of the equity interests of JCR Soft Company Limited for fixed cash consideration of \$350,000. As the Group does not have significant influence over JCR Soft, the Group accounts for the equity investment using the cost method. The Group’s management reviewed the Group’s equity investments for impairment in accordance with ASC 320 Investments-Debt and Equity Securities (ASC 320), 320-10-35, Subsequent Measurement, and concluded that the estimated fair value of the investment in JSR Soft is significantly less than its carrying value and, therefore, the Group provided for an impairment loss of \$350,000 to reduce the carrying value of this investment to \$nil.

In 2012, the Group acquired 10% of the equity interests of Bridea Corporation for fixed cash consideration of \$500,000. As the Group does not have significant influence over Bridea Corporation, the Group accounts for the equity investment using the cost method. We recorded a full impairment of our investment in Bridea for the year ended December 31, 2013.

## 13. GOODWILL

In 2013, for the reporting units of the MMOG business, the Web game business, the 17173 Business and the cinema advertising business, the Company qualitatively assessed whether it is more likely than not that the fair values of these reporting units were less than their carrying amounts. The MMOG business and the Web game business are aggregated and presented as the online game business reporting unit.

The changes in the carrying value of goodwill are as follows:

	Online Game (in thousands)	17173 Business (in thousands)	Others (in thousands)	Total (in thousands)
Balance as of December 31, 2012				
Goodwill	\$ 116,992	\$ 17,929	\$ 5,201	\$ 140,122
Accumulated impairment losses	—	—	(5,201)	(5,201)
	<u>\$ 116,992</u>	<u>\$ 17,929</u>	<u>\$ —</u>	<u>\$ 134,921</u>
Transactions in 2013				
Acquisitions	\$ 33,740	\$ 7,626	\$ —	\$ 41,366
Foreign exchange	3,363	602	—	3,965
Balance as of December 31, 2013				
Goodwill	\$ 154,095	\$ 26,157	\$ 5,201	\$ 185,453
Accumulated impairment losses	—	—	(5,201)	(5,201)
	<u>\$ 154,095</u>	<u>\$ 26,157</u>	<u>\$ —</u>	<u>\$ 180,252</u>

For the qualitative analysis performed for the MMOG business, the Web game business and the online advertising business, the Company took into consideration all the events and circumstances listed in ASC350, Intangibles—Goodwill and Other, in addition to other entity specific factors. Based on the assessment, the Company determined that it was not necessary to perform a quantitative goodwill impairment test for the MMOG business, the Web game business and the online advertising business. In addition, Doyo and the RaidCall Business were acquired in November and December 2013, respectively. Since Doyo primarily engages in the online advertising and traffic monetization business, which has similar economic characteristics to the 17173 Business, the 17173 Business and Doyo are aggregated as a reporting unit. The RaidCall Business will be aggregated with the Company's online game segment as one reporting unit, since the RaidCall Business's communications tool is expected to enhance playing experience of the Company's game players.

After completing its annual impairment reviews for each reporting unit on an annual basis as of October 1, 2013, the Company concluded that goodwill was not impaired. Management is not aware of the occurrence any significant events or changes in circumstances from the assessment date to December 31, 2013 that would be more likely than not to reduce the fair values of the reporting units below their carrying values.

#### 14. OTHER ASSETS, NET:

	As of December 31, (in thousands)	
	2012	2013
Prepayment for an office building	\$126,004	\$ —
Prepayment for Sohu services	10,138	259
Deferred tax assets, net	2,771	958
Employee advance	—	4,796
Accrued interest income	2,229	1,132
Others	661	915
<b>Total</b>	<b>\$141,803</b>	<b>\$8,060</b>

In August 2010, the Group entered into a contract for the purchase and development of an office building of approximately 56,549 square meters in Beijing to serve as its headquarters. In accordance with the contract, the Group had paid \$126.0 million to the property developer through December 31, 2012. The Group put the office building in service in December 2013.



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## 15. FAIR VALUE MEASUREMENT

The following table sets forth the financial instruments, measured at fair value, by level within the fair value hierarchy as of December 31, 2012 and 2013:

Items	As of December 31, 2013	Fair value measurement at reporting date using (in thousands)		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents	\$ 10,388	\$ —	\$ 10,388	\$ —
Restricted time deposits	424,674	—	424,674	—
Short-term investments	2,827	—	2,827	—
<b>Total</b>	<b>\$ 437,889</b>	<b>\$ —</b>	<b>\$ 437,889</b>	<b>\$ —</b>

Items	As of December 31, 2012	Fair value measurement at reporting date using (in thousands)		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents	\$ 178,059	\$ —	\$ 178,059	\$ —
Restricted time deposits	246,599	—	246,599	—
Short-term investments	51,720	—	51,720	—
<b>Total</b>	<b>\$ 476,378</b>	<b>\$ —</b>	<b>\$ 476,378</b>	<b>\$ —</b>

### Cash equivalents

The Company's cash equivalents include time deposits with maturities of three months or less. These time deposits are classified within Level 2, because there generally were no quoted prices as of the reporting dates in active markets for identical time deposits and therefore, in order to determine their fair value, the Company had to use the discounted cash flow method and observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that were observable or could be corroborated by observable market data for substantially the full term of the assets or liabilities.

As of December 31, 2012 and 2013, the Company's cash equivalents included time deposits with maturities of three months or less amounting to \$178.1 million and \$10.4 million, respectively.

### Restricted time deposits

Restricted time deposits are valued based on the prevailing interest rates in the market using the discounted cash flow method. The Company classifies the valuation techniques that use these inputs as Level 2 of fair value measurements.

### Short-term investments

To estimate the fair value of investments in financial instruments with a variable interest rate indexed to the performance of underlying assets, the Company refers to the quoted rate of return provided by banks at the end of each period using the discounted cash flow method. The Company classifies the valuation techniques that use these inputs as Level 2 of fair value measurement.

As of December 31, 2012 and 2013, the Company's investments in financial instruments were approximately \$51.7 million and \$2.8 million, respectively. The financial instruments are issued by commercial banks in China with a variable interest rate indexed to the performance of underlying assets. Since the maturity dates of these financial instruments are within one year, the investments are classified as short-term investments.



The following are other financial instruments not measured at fair value in the balance sheets but for which the fair value is estimated for disclosure purposes.

#### *Short-term receivables and payables*

Accounts receivable and prepaid and other current assets are financial assets with carrying values that approximate fair value due to their short term nature. Short-term accounts payable, receipts in advance and deferred revenue, short-term bank loans and accrued liabilities are financial liabilities with carrying values that approximate fair value due to their short term nature. The rates of interest under the loan agreements with the lending banks were determined based on the prevailing interest rates in the market. The Company classifies the valuation techniques that use these inputs as Level 2 of fair value measurements of short-term bank loans. The Company estimated fair values of other short-term receivables and payables using the discounted cash flow method. The Company classifies the valuation technique as Level 3 of fair value measurement, as it uses estimated cash flow input which is unobservable in the market.

#### *Long-term prepayment and other non-current assets and long-term payables*

Long-term prepayment and other non-current assets are financial assets with carrying values that approximate fair value due to the change in fair value after considering the discount rate, being immaterial. Long-term account payable are financial liabilities with carrying values that approximate fair value due to the change in fair value after considering the discount rate, being immaterial. The rates of interest under the Company's loan agreements with the lending banks were determined based on the prevailing interest rates in the market. The Company classifies the valuation techniques that use these inputs as Level 2 of fair value measurements of long-term bank loans. The Company estimated fair values of long-term prepayment in non-current assets and long-term account payable using the discounted cash flow method. The Company classifies the valuation technique as Level 3 of fair value measurement, as it uses estimated cash flow input which is unobservable in the market.

### 16. RECEIPTS IN ADVANCE AND DEFERRED REVENUE

	As of December 31, (in thousands)	
	2012	2013
Receipts in advance	\$15,074	\$13,142
Deferred revenue	28,585	30,700
<b>Total</b>	<b>\$43,659</b>	<b>\$43,842</b>

### 17. OTHER ACCRUED LIABILITIES

	As of December 31, (in thousands)	
	2012	2013
Consideration payable for business acquisitions	\$19,658	\$ 2,820
Customer deposits	5,258	3,807
Advance from government grants	3,007	3,479
Accrued transaction costs for acquisition of the 17173 Business	1,541	1,670
Others	2,695	3,096
<b>Total</b>	<b>\$32,159</b>	<b>\$14,872</b>

### 18. SHARE-BASED COMPENSATION

#### *Share Awards Granted before Initial Public Offering*

##### *Share-based compensation allocated from Sohu to the Company*

The 2000 Stock Incentive Plan of the Company's ultimate parent company, Sohu.com, provides for the issuance of stock options and restricted stock units to purchase up to 9,500,000 shares of common stock to qualified employees. The maximum term of any issued stock right is ten years from the grant date.





In determining the fair value of share options granted by Sohu to employees of Changyou, the Company applied the Black-Scholes valuation model. Restricted share units granted by Sohu to employees of Changyou were measured based on the fair market value of the underlying stock on the dates of grants.

There was no grant of stock options by Sohu to Changyou employees during 2011, 2012 or 2013.

A summary of option activity, relating to options held by employees of the Predecessor Operations under Sohu's 2000 Stock Incentive Plan as of December 31, 2013 and changes during the year then ended, is presented below:

Options	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at January 1, 2013	5	19.12	2.31	141
Exercised	(2)	21.63		
Outstanding at December 31, 2013	3	17.71	1.46	177
Vested at December 31, 2013	3	17.71	1.46	177
Exercisable at December 31, 2013	3	17.71	1.46	177

The aggregate intrinsic value in the preceding table represents the total intrinsic value based on the closing price on December 31, 2013 of shares of Sohu.com Inc. common stock on NASDAQ of \$72.93

The total fair values of options expensed during the years ended December 31, 2011, 2012 and 2013 were \$ nil, \$nil and \$nil, respectively. The total intrinsic values of options exercised during the years ended December 31, 2011, 2012 and 2013 were \$173,000, \$110,000 and \$74,000, respectively. As of December 31, 2013, there was no unrecognized compensation expense for options because the requisite service periods for the remaining options had been satisfied on or prior to that date.

As of December 31, 2013, there was \$nil of unrecognized compensation expenses related to unvested restricted stock units, net of estimated forfeitures. The total fair values of restricted stock units expensed during the years ended December 31, 2011, 2012 and 2013 were \$31,000, \$130,000 and \$nil, respectively.

The total fair value of vested restricted stock units on their respective vesting dates during the years ended December 31, 2011, 2012 and 2013 were \$88,000, \$57,000 and \$nil, respectively.

There were no capitalized share-based compensation costs during the years ended December 31, 2011, 2012 and 2013.

The maximum term of any issued stock right under the Sohu 2000 Stock Incentive Plan is ten years from the grant date. The Sohu 2000 Stock Incentive Plan expired on January 24, 2010 and a new plan was adopted on July 2, 2010. As of the expiration date, 9,128,724 shares of common stock had been issued or were subject to issuance upon the vesting and exercise of share options or the vesting and settlement of restricted share units granted under the plan.

#### *Share-based compensation allocated from Sohu to the 17173 Business*

A summary of option activity, relating to options held by employees of the 17173 Business under Sohu's 2000 Stock Incentive Plan as of December 31, 2013, and changes during the year then ended, is presented below:

Options	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at January 1, 2013	7	20.30	2.13	198
Exercised	(4)	22.41		
Outstanding at December 31, 2013	3	17.61	1.36	178
Vested at December 31, 2013	3	17.61	1.36	178
Exercisable at December 31, 2013	3	17.61	1.36	178

The aggregate intrinsic value in the preceding table represents the total intrinsic value based on the closing price on December 31, 2013 of shares of Sohu.com common stock on NASDAQ of \$72.93. The total intrinsic value of share options exercised for the year ended December 31, 2013 was \$171,000.



No options have been granted under Sohu's 2000 Stock Incentive Plan since 2006. For the years ended December 31, 2011, 2012 and 2013, no share-based compensation expense was recognized for share options because the requisite service periods for share options had ended by the end of 2009.

A summary of restricted stock unit activity, relating to restricted stock units held by employees of the 17173 Business under Sohu's 2000 Stock Incentive Plan as of December 31, 2013, and changes during the year then ended, is presented below:

<u>Restricted Share Units</u>	<u>Number of Units (in thousands)</u>	<u>Weighted-Average Grant-Date Fair Value</u>
Unvested at January 1, 2013	8	\$ 61.27
Vested	(4)	61.27
Forfeited	(1)	61.27
Unvested at December 31, 2013	3	61.27
Expected to vest thereafter	2	61.27

As of December 31, 2013, there was \$4,000 of unrecognized compensation expenses related to unvested restricted stock units, net of estimated forfeitures. This amount is expected to be recognized over a weighted average period of 0.25 years. The total fair values of restricted stock units granted to employees expensed during the years ended December 31, 2011, 2012 and 2013 were \$321,000, \$173,000 and \$76,000, respectively.

The total fair value of vested restricted stock units on their respective vesting dates during the years ended December 31, 2011, 2012 and 2013 were \$405,000, \$353,000 and \$182,000, respectively.

The total fair values of options and restricted stock units expenses relating to Sohu's senior management allocated to the 17173 Business during the years ended December 31, 2011, 2012 and 2013 were \$218,000, \$ nil and \$nil, respectively.

There were no capitalized share-based compensation costs during the years ended December 31, 2011, 2012 and 2013.

#### Changyou 2008 Share Incentive Plan

On December 31, 2008, the Company reserved 2,000,000 of its ordinary shares, which included 1,774,000 Class B ordinary shares and 226,000 Class A ordinary shares, for issuance to certain of its executive officers and employees as incentive compensation under the Company's 2008 Share Incentive Plan (the "Changyou 2008 Share Incentive Plan").

The Company's ordinary shares are divided into Class A ordinary shares and Class B ordinary shares. Holders of Class A ordinary shares and holders of Class B ordinary shares have the same rights in the Company, with the exception of voting and conversion rights. Each Class A ordinary share is entitled to one vote on all matters subject to a shareholder vote, and each Class B ordinary share is entitled to ten votes on all matters subject to a shareholder vote. Each Class B ordinary share is convertible into one Class A ordinary share at any time at the election of the holder. Class A ordinary shares are not convertible into Class B ordinary shares under any circumstances.

In March 2009, the 2,000,000 reserved ordinary shares were subject to a ten-for-one share split and became 20,000,000 ordinary shares.

Through December 31, 2013, the Company had granted under the Changyou 2008 Share Incentive Plan 15,000,000 Class B ordinary shares to Tao Wang, Chief Executive Officer of Changyou, through Prominence Investments Ltd. ("Prominence") and 4,823,552 Class A and/or Class B restricted share units (setttable by issuance of Class A ordinary shares or Class B ordinary shares, respectively) to certain of its executive officers other than Tao Wang and to certain of its employees and certain Sohu employees. Prominence is an entity that may deemed under applicable rules of the Securities and Exchange Commission ("SEC") to be beneficially owned by Tao Wang.

In determining the fair value of ordinary shares, restricted shares and restricted share units granted by the Company in January and April 2008, the income approach/discounted cash flow method with a discount for lack of marketability was applied given that the shares underlying the awards were not publicly traded at the time of grant.

Determining the fair value of the ordinary shares of the Company required complex and subjective judgments regarding its projected financial and operating results, its unique business risks, the liquidity of its ordinary shares and its operating history and prospects at the time the grants were made.



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Because at the time of the grants the Company's business was at a different stage of its product life cycle than that of the publicly listed companies in the online game industry, it was concluded that a market comparison approach would not have been meaningful in determining the fair value of the Company's ordinary shares. As a result, the Company used the income approach/discounted cash flow method to derive the fair values. The Company applied the discounted cash flow, or DCF, analysis based on the Company's projected cash flow using management's best estimate as of the respective valuation dates. The projected cash flow estimate included, among other things, an analysis of projected revenue growth, gross margins, effective tax rates, capital expenditures and working capital requirements. The income approach involves applying appropriate discount rates, based on earnings forecasts, to estimated cash flows. The assumptions the Company used in deriving the fair value of its ordinary shares were consistent with the assumptions used in developing its MMORPG business plan, which included no material changes in the existing political, legal, fiscal and economic conditions in China; its ability to recruit and retain competent management, key personnel and technical staff to support its ongoing operations; and no material deviation in industry trends and market conditions from economic forecasts. These assumptions are inherently uncertain and subjective. The discount rates reflect the risks the management perceived as being associated with achieving the forecasts and are based on the Company's estimated cost of capital, which was derived by using the capital asset pricing model, after taking into account systemic risks and company-specific risks. The capital asset pricing model is a model for pricing securities that adds an assumed risk premium rate of return to an assumed risk-free rate of return. Using this method, the Company determined the appropriate discount rates to be 22% as of the January 2008 valuation date and 23% as of the April 2008 valuation date.

The Company also applied a discount for lack of marketability, or DLOM, to reflect the fact that, at the time of the grants, Changyou.com Limited was a closely-held company and there was no public market for its ordinary shares. To determine the discount for lack of marketability, the Company used the Black-Scholes option pricing model. Pursuant to the Black-Scholes option pricing model, the Company used the cost of a put option, which can be used to hedge the price change before a privately held share can be sold, as the basis to determine the discount for lack of marketability. Based on the foregoing analysis, the Company used a DLOM of 19% to discount the value of the Changyou's ordinary shares as of the January 2008 and April 2008 valuation dates.

Because there was no evidence to indicate that there would be a disproportionate return between majority and minority shareholders, the Company did not apply a minority discount. As a result, it was concluded that the fair value of Changyou.com Limited as a going concern was \$136 million as of the January 2008 valuation date and \$198 million as of the April 2008 valuation date.

In determining the fair value of restricted share units granted in 2009 before the Company's initial public offering, the fair value of the underlying shares was determined based on the offering price of ADSs in the offering. In determining the fair value of restricted share units granted after the initial public offering, the fair value is determined based on the market price of the Company's ADSs on the grant dates.

Share-based compensation expense for ordinary shares granted is fully recognized in the quarter during which these ordinary shares are granted. Share-based compensation expense for share options, restricted shares and restricted share units granted is recognized on an accelerated basis over the requisite service period. The number of share-based awards for which the service is not expected to be rendered over the requisite period is estimated, and the related compensation expense is not recorded for that number of awards.

The assumptions used in share-based compensation expense recognition represent management's best estimates based on historical experience and consideration to developing expectations about the future. These estimates involve inherent uncertainties and the application of management judgment, however. If factors change or different assumptions are used, the share-based compensation expense could be materially different for any period. Moreover, the estimates of fair value are not intended to predict actual future events or the value that ultimately will be realized by employees who receive equity awards, and subsequent events are not indicative of the reasonableness of the original estimates of fair value made by the Company for accounting purposes.

For the years ended December 31, 2011, 2012 and 2013, total share-based compensation expense recognized for awards under the Changyou 2008 Share Incentive Plan was \$5.5 million, \$3.4 million and \$1.2 million, respectively.

For Changyou restricted shares granted to Tao Wang and restricted share units granted to senior management and certain key employees before Changyou's initial public offering, there was no unrecognized share-based compensation expense as of December 31, 2013, as these awards were fully vested in 2012.

#### *Share awards to other employees*

On February 17, 2009, the Company granted an aggregate of 456,000 Class A restricted share units to certain of its employees. These restricted share units are subject to vesting over a four-year period commencing upon the completion of the listing of the Company's Class A ordinary shares in an initial public offering.

A summary of restricted share units activity as of and for the year ended December 31, 2013, is presented below:

<u>Restricted Share Units</u>	<u>Number of Units (in thousands)</u>	<u>Weighted-Average Grant-Date Fair Value</u>
Unvested at January 1, 2013	81	\$ 8.00
Vested	(81)	8.00
Unvested at December 31, 2013	—	
Expected to vest thereafter	—	

Share-based compensation expense relating to the 456,000 Class A restricted share units for the years ended December 31, 2011, 2012 and 2013 was \$0.6 million, \$0.3 million and negative \$0.3 million, respectively. The negative \$0.3 million represents Changyou's true-up of the share-based compensation expense for restricted share units forfeited in 2013. As of December 31, 2013, there was no unrecognized compensation expense related to 456,000 Class A restricted share units of the Company granted to employees before the initial public offering.

The total fair values of restricted stock units vested on their respective vesting dates during the years ended December 31, 2011, 2012 and 2013 were \$1.6 million, \$1.2 million and \$1.1 million, respectively.

### *Share Awards Granted after Initial Public Offering*

#### **Changyou 2008 Share Incentive Plan**

#### *Share-based compensation to senior management and Changyou employees*

On April 21, 2009, the Company granted an aggregate of 1,200,000 Class A restricted share units (setttable upon vesting in Class A ordinary shares) to executive officers other than the CEO. These Class A restricted share units are subject to vesting over a four-year period commencing on April 21, 2009. The fair value as of April 21, 2009, the grant date of restricted share units, was determined based on the Company's share price on the grant date.

As of December 31, 2013, the Company had granted an aggregate of 367,552 Class A restricted share units (setttable upon vesting in Class A ordinary shares) to certain employees. These Class A restricted share units are subject to vesting over a four-year period commencing on grant dates. The fair values as of grant dates of restricted share units were determined based on the Company's share price on the grant dates.

A summary of restricted share unit activity with respect to grants under the Changyou 2008 Share Incentive Plan as of and for the year ended December 31, 2013 is presented below:

<u>Restricted Share Units</u>	<u>Number of Units (in thousands)</u>	<u>Weighted-Average Grant-Date Fair Value</u>
Unvested at January 1, 2013	502	\$ 13.08
Granted	78	14.40
Vested	(365)	12.73
Forfeited	(10)	12.11
Unvested at December 31, 2013	205	14.26
Expected to vest thereafter	193	14.26

Share-based compensation expense recognized for restricted share units for the years ended December 31, 2011, 2012 and 2013 under the Changyou 2008 Share Incentive Plan was \$3.5 million, \$2.8 million and \$1.4 million, respectively. As of December 31, 2013, there was \$1.2 million of unrecognized compensation expense related to unvested restricted share units. The expense is expected to be recognized over a weighted average period of 1.06 years.

The total fair values of restricted stock units vested on their respective vesting dates during the years ended December 31, 2011, 2012 and 2013 were \$6.1 million, \$4.6 million and \$5.3 million, respectively.

#### *Share Awards to Employees of the 17173 Business*

On October 24, 2010 and January 29, 2011, the Company granted 40,000 and 20,000 Class A restricted share units (setttable upon vesting in Class A ordinary shares), respectively, to certain employees of the 17173 Business, which was then owned and operated by Sohu, for their involvement in the provision of certain online game links and advertising services to the Company on its Websites.



These Class A restricted share units are subject to vesting over a four-year period commencing on the grant date. Since its acquisition of the 17173 Business on December 15, 2011, the Company has accounted for the Class A restricted share units to employees of the 17173 Business as if they were employees of the Company from the beginning of the period. The fair values of these share awards were determined based on the Company's share price on the grant dates.

A summary of restricted share units to employees of the 17173 Business as of and for the year ended December 31, 2013 is presented below:

Restricted Share Units	Number of Units (in thousands)	Weighted-Average Fair Value
Unvested at January 1, 2013	24	\$ 17.75
Vested	(10)	17.80
Forfeited	(1)	18.00
Unvested at December 31, 2013	13	17.68
Expected to vest thereafter	12	17.68

Share-based compensation expense relating to these 60,000 Class A restricted share units for the years ended December 31, 2011, 2012 and 2013 was \$0.5 million, \$0.3 million and \$0.1 million, respectively. As of December 31, 2013, there was \$61,000 of unrecognized compensation expense related to unvested restricted share units. The expense is expected to be recognized over a weighted average period of 0.58 years.

The total fair values of restricted share units vested on their respective vesting dates during the years ended December 31, 2011, 2012 and 2013 were \$0.2million, \$0.2 million and \$0.2 million, respectively.

#### 7Road 2012 Share Incentive Plan

On July 10, 2012, 7Road Cayman adopted a 2012 Share Incentive Plan (the "7Road 2012 Share Incentive Plan"), which initially provided for the issuance to selected directors, officers, employees, consultants and advisors of 7Road of up to 5,100,000 ordinary shares of 7Road Cayman (amounting to 5.1% of the then outstanding 7Road Cayman shares on a fully-diluted basis). On November 2, 2012, 7Road Cayman's Board of Directors and its shareholders approved an increase from 5,100,000 to 15,100,000 ordinary shares (amounting to 13.7% of the then outstanding 7Road Cayman shares on a fully-diluted basis) under the 7Road 2012 Share Incentive Plan.

On May 1, 2013, Changyou entered into an agreement to acquire all of the outstanding ordinary shares of 7Road Cayman held by non-controlling shareholders. The acquisition closed on June 5, 2013.

On June 28, 2013, 7Road Cayman's Board of Directors approved the cancellation of the 7Road 2012 Share Incentive Plan. 7Road Cayman concurrently offered to a total of 42 7Road employees holding an aggregate of 2,223,750 restricted share units which had been granted under the 7Road 2012 Share Incentive Plan the right to exchange their restricted share units for, at each employee's election, in each case subject to the employee's continued employment by 7Road, either (i) Scheme I: the right to a cash payment of up to an aggregate of \$2.90 per restricted share unit exchanged, vesting and payable at the rate of 40%, 30% and 30%, respectively, on the first, second and third anniversaries of July 18, 2012, which is the date when the surrendered restricted share units were granted under the 7Road 2012 Share Incentive Plan, or (ii) Scheme II: the right to receive an annual cash bonus, over a seven-year period commencing July 1, 2013, based on adjusted annual cumulative net income of 7Road. All restricted share units held by these 42 holders under the 7Road 2012 Share Incentive Plan as of June 28, 2013 were included in this exchange program.

As the original awards of restricted share units made under the 7Road 2012 Share Incentive Plan included as a vesting condition the completion of an IPO, which is not considered probable under it occurs, no share-based compensation expense was recognized for the fair value of the original awards. As of the date of the modification resulting from the exchange program, incremental compensation expense, which is not classified as share-based compensation expense, will be the fair values of the two new compensation schemes included in the exchange program.

For Scheme I, the modification resulted in total incremental compensation expense of \$5.7 million, which will be recognized in the consolidated statements of comprehensive income ratably over the remaining vesting period of the awards for each tranche. For fiscal year 2013, compensation expense of \$3.3 million was recognized in the consolidated statements of comprehensive income. As of December 31, 2013, 7Road paid \$1.6 million in cash bonuses under Scheme I.





For Scheme II, the incremental compensation expense varies depending on 7Road's financial performance. In the third quarter of 2013, 7Road granted to an additional 48 7Road employees the right to receive an annual cash bonus under Scheme II with the same terms as described above. For the fiscal year 2013, compensation expense of \$0.4 million was recognized in the consolidated statements of comprehensive income.

## 19. MEZZANINE EQUITY

On May 11, 2011, the Company, through Gamease, acquired 68.258% of the equity interests of 7Road and began to consolidate 7Road's financial statements on June 1, 2011.

Mezzanine Equity consists of non-controlling interest in 7Road and a put option pursuant to which the non-controlling shareholders will have the right to put their equity interests in 7Road to the Company at a pre-determined price if 7Road achieves specified performance milestones before the expiry of the put option and 7Road does not complete an initial public offering on NASDAQ, the New York Stock Exchange or The Stock Exchange of Hong Kong. The put option will expire in 2014. Since the occurrence of the sale is not solely within the control of the Company, the Company classifies the non-controlling interest as mezzanine equity instead of permanent equity in the Company's consolidated financial statements.

In accordance with ASC subtopic 480-10, the Company calculates, on an accumulative basis from the acquisition date, (i) the amount of accretion that would increase the balance of non-controlling interest to its estimated redemption value over the period from the date of the 7Road acquisition to the earliest redemption date of the non-controlling interest and (ii) the amount of net profit attributable to non-controlling shareholders of 7Road based on their ownership percentage. The carrying value of the non-controlling interest as mezzanine equity will be adjusted by an accumulative amount equal to the higher of (i) and (ii).

On May 1, 2013, Changyou entered into an agreement to acquire all of the ordinary shares of 7Road Cayman held by the non-controlling shareholders. The acquisition closed on June 5, 2013. Under ASC 810-10, changes in a parent's ownership interest while the parent retains control of its subsidiary are accounted for as equity transactions, and do not impact net income or comprehensive income in the consolidated financial statements. Following the closing of the acquisition, \$2.4 million, representing the excess of the amount of the mezzanine-classified non-controlling interest in 7Road Cayman over the purchase price as of the closing date, was recorded in the equity accounts.

For the year ended December 31, 2013, an accretion charge of \$17.8 million, compared to \$11.2 million for the year ended December 31, 2012, was recorded as net income attributable to the mezzanine classified non-controlling interest shareholders in the statements of comprehensive income.

## 20. TAXATION

### *a. Transition from PRC Business Tax to PRC Value Added Tax*

The Pilot Program for transition from the imposition of Business Tax to the imposition of VAT for revenues from certain industries was launched in Shanghai on January 1, 2012. Effective September 1, 2012, the Pilot Program was expanded from Shanghai to eight other cities and provinces in China, including Beijing.

Cinema advertising revenues became subject to VAT on January 1, 2012 and online advertising revenues became subject to VAT on September 1, 2012, at a rate of 6%.

Effective December 1 2012, revenues derived from the operation of Web games that were not developed in-house became subject to VAT at a rate of 6%.

### *b. Business Tax and related Surcharges*

Prior to the Pilot Program, the Group was subject to a 5% Business Tax and 0.6% in related surcharges on revenues from MMOG operations, the online advertising business in the PRC, and the cinema advertising business in the PRC. Business Tax and the related surcharges are recognized when the revenue is earned.

After the Pilot Program, the Company's MMOG operations remain subject to Business Tax and the related surcharges.

### *c. VAT*

Prior to the Pilot Program, in addition to Business Tax and related surcharges, the Group was subject to VAT at an effective rate of 3% for revenues from intra group software sales in the PRC. In 2011, with the consolidation of 7Road, VAT was imposed on its in-house-developed Web game revenue at a rate of 17%, with a 14% immediate tax refund, resulting in a net rate of 3% plus a related surcharge of 2% on such revenue.



After the Pilot Program, the Group's online advertising and cinema advertising revenues are subject to VAT at a rate of 6%.

There is an additional culture construction fee surcharge of 3% on revenues from the online advertising and cinema advertising businesses. In addition, entities incorporated in Beijing were subject to a surcharge of 0.72% on their revenues for the year ended December 31, 2013.

#### **d. Income tax**

##### *Cayman Islands*

Under the current tax laws of the Cayman Islands, the Company is not subject to tax on its income or capital gains. In addition, upon payment of dividends by the Company to its shareholders, no Cayman Islands withholding tax will be imposed.

##### *Hong Kong*

Entities incorporated in Hong Kong are subject to profits tax in Hong Kong at the rate of 16.5% for each of the years ended December 31, 2011, 2012 and 2013.

##### *China*

The Company's subsidiaries and VIEs in China are governed by the Corporate Income Tax Law ("CIT Law"), which became effective on January 1, 2008. Pursuant to the CIT Law and its implementation rules, enterprises in China are generally subject to tax at a statutory rate of 25%, certain High and New Technology Enterprises are entitled to a favorable statutory tax rate of 15%, and Software Enterprises can enjoy an income tax exemption for two years beginning with their first profitable year and a 50% tax reduction to a rate of 12.5% for the subsequent three years. Both AmazGame and Gamease are qualified as software enterprises and were subject to a 50% tax reduction to a rate of 12.5% from fiscal year 2009 to fiscal year 2011. Both AmazGame and Gamease were approved as High and New Technology Enterprises in September 2011 and enjoyed a preferential income tax rate of 15% for 2012 and 2013. In addition, AmazGame is qualified as a "Key National Software Enterprise" for 2013 and 2014 and will enjoy a further reduced preferential tax rate of 10% for those years. Gamespace qualified as a software enterprise and was entitled to an income tax exemption for the fiscal years 2012 and 2013 and will be entitled to a 50% tax reduction to a rate of 12.5% for the subsequent three years.

Shenzhen 7Road is qualified as a software enterprise and was entitled to an income tax exemption for the fiscal years 2009 and 2010 and a 50% tax reduction to a rate of 12.5% for the subsequent three years. Shanghai ICE is qualified as a software enterprise and was entitled to an income tax exemption for the fiscal years 2010 and 2011 and a 50% tax reduction to a rate of 12.5% for the subsequent three years. ICE Information and 7Road Technology are qualified as software enterprises and are entitled to an income tax exemption for two years beginning with their first profitable year and a 50% tax reduction for the subsequent three years, if they continue to maintain the qualifications. 7Road Technology was profitable in 2013 and enjoyed an income tax exemption for that year.

The license fees and royalties received from licensees in various jurisdictions outside of the PRC are subject to foreign withholding taxes. The Group recognizes such foreign withholding taxes as income tax expense when the related license fee and royalty revenue is recognized.

Under the CIT Law and its implementation rules, the profits of a foreign invested enterprise arising in 2008 and onwards which are distributed to its immediate holding company outside the PRC will be subject to a withholding tax rate of 10%. A lower withholding tax rate will be applied if there is a tax treaty between the PRC and the jurisdiction of the foreign holding company. A holding company in Hong Kong, for example, will be subject to a 5% withholding tax rate under the Arrangement between the PRC and the Hong Kong Special Administrative Region on the Avoidance of Double Taxation and Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital (the "China-HK Tax Arrangement") if such holding companies is considered a non-PRC resident enterprises and holds at least 25% of the equity interests in the PRC foreign invested enterprise distributing the dividends, subject to approval of the PRC local tax authority. However, if the Hong Kong holding company is not considered to be the beneficial owner of such dividends under applicable PRC tax regulations, such dividend may remain subject to withholding tax rate of 10%.



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On October 27, 2009, the PRC State Administration of Taxation issued Circular 601, which provides guidance on determining whether an enterprise is a beneficial owner under China's tax treaties and tax arrangements. If any of the Company's Hong Kong subsidiaries is, in the light of Circular 601, to be considered a non-beneficial owner for purpose of the China-HK Tax Arrangement, any dividends paid to it by any of the Company's PRC subsidiaries would not qualify for the preferential dividend withholding tax rate of 5%, but rather would be subject to the usual New CIT Law rate of 10%. In order to fund the distribution of a dividend to the Company's shareholders, the Company's board of directors determined to cause one of the Group's PRC subsidiaries to declare and distribute a cash dividend of all of its stand-alone 2012 earnings and half of its stand-alone 2013 earnings to its direct overseas parent company, Changyou HK. The Company does not intend to cause any of its PRC subsidiaries to distribute any profits of such subsidiaries with respect to years prior to 2012 to their direct overseas parent companies, but rather intends that such profits will be retained by such subsidiaries for their PRC operations. Under the corporate income tax law and relevant rules, such dividend out of earnings generated after January 1, 2012 is subject to a 5% withholding tax. Therefore, withholding tax associated with this distribution plan was accrued and recorded as deferred tax liabilities in the amount of \$18.8 million as of December 31, 2013.

For the years ended December 31, 2011, 2012 and 2013, the Company did not have any material interest or penalties associated with tax positions nor did the Company have any significant unrecognized uncertain tax positions.

### Composition of income tax expense

The current and deferred portions of income tax expense included in the consolidated statements of comprehensive income are as follows:

	For the year ended December 31, (in thousands)		
	2011	2012	2013
Loss from foreign entities	\$ (13,211)	\$ (17,283)	\$ (35,175)
Income from PRC entities	304,805	378,284	357,980
Income before income tax expenses	\$291,594	\$361,001	\$322,805
Current income tax expense	\$ 43,548	\$ 55,995	\$ 28,909
Deferred tax	(1,462)	9,718	5,382
Income tax expenses applicable to PRC entities	\$ 42,086	\$ 65,713	\$ 34,291
Foreign withholding tax expense	1,494	1,692	2,092
<b>Income tax expense</b>	<b>\$ 43,580</b>	<b>\$ 67,405</b>	<b>\$ 36,383</b>

Reconciliation between the statutory CIT rate and the Group's effective tax rate is as follows:

	For the year ended December 31,		
	2011	2012	2013
Statutory CIT rate	25.0%	25.0%	25.0%
Effect of tax holidays	(16.1)%	(10.9)%	(19.5)%
Effect of withholding taxes	0.5%	3.7%	2.7%
Changes in valuation allowance	3.2%	2.6%	2.4%
Other permanent book-tax differences	2.3%	(1.7)%	0.7%
<b>Effective CIT rate</b>	<b>14.9%</b>	<b>18.7%</b>	<b>11.3%</b>

The combined effects of the income tax expense exemption and reduction available to the Group are as follows (in thousands, except per share data):

	For the year ended December 31,		
	2011	2012	2013
Tax holiday effect	\$46,910	\$39,451	\$62,893
Basic earnings per share	\$ 0.45	\$ 0.37	\$ 0.59

*e. Deferred tax assets and liabilities*

Significant components of the Group's deferred tax assets consist of the following:

	As of December 31, (in thousands)	
	2012	2013
Deferred tax assets		
Net operating loss from operations	\$ 25,571	\$ 33,830
Intangible assets	3,183	2,775
Accrued salary and benefits	4,538	5,366
Others	2,335	2,194
Total deferred tax assets	35,627	44,165
Less: Valuation allowance	(30,627)	(38,464)
Net deferred tax assets	\$ 5,000	\$ 5,701
Deferred tax liability		
Related to acquired intangible assets	\$ 3,846	\$ 8,301
Withholding tax related to distribution of dividend	11,878	18,814
VAT refund	3,978	4,033
Net deferred tax liabilities	\$ 19,702	\$ 31,148

As of December 31, 2012 and 2013, the Group has made a valuation allowance against its deferred tax assets to the extent such deferred tax assets are not expected to be realized by certain subsidiaries and VIEs. The Group evaluated a variety of factors in determining the amount of the valuation allowance, including the Group's limited operating history and uncertainty as to the success of the Group's businesses due to intense competition in the industries in which the Group operates its businesses.

**21. CHINA CONTRIBUTION PLAN**

The Company's subsidiaries and VIEs in the PRC participate in a government-mandated multi-employer defined contribution plan pursuant to which certain retirement, medical and other welfare benefits are provided to employees. Chinese labor regulations require the Company's subsidiaries and VIEs in the PRC to pay to the local labor bureau a monthly contribution at a stated contribution rate based on the monthly compensation of qualified employees. The relevant local labor bureau is responsible for meeting all retirement benefit obligations; the Group has no further commitments beyond its monthly contribution. During the years ended December 31, 2011, 2012 and 2013, the Group contributed approximately a total of \$14.4 million, \$20.5 million and \$30.1 million, respectively, to these funds.

**22. STATUTORY RESERVES**

The Company's China-based subsidiaries and VIEs are required to make appropriations to certain non-distributable reserve funds.

Pursuant to the China Foreign Investment Enterprises laws, some of the Company's China-based subsidiaries, which are called wholly foreign-owned enterprises ("WFOEs"), have to make appropriations from their after-tax profit as determined under generally accepted accounting principles in the PRC (the "after-tax-profit under PRC GAAP") to non-distributable reserve funds, including (i) general reserve fund, (ii) enterprise expansion fund, and (iii) staff bonus and welfare fund. Each year, at least 10% of the after-tax-profit under PRC GAAP is required to be set aside as general reserve fund until such appropriations for the fund equal 50% of the paid-in capital of the applicable entity. The appropriation for the other two reserve funds is at the Company's discretion as determined by the Board of Directors of each entity.

Pursuant to the China Company Laws, some of the Company's China-based subsidiaries, which are called domestically funded enterprises, as well as the Company's VIEs, have to make appropriations from their after-tax-profit under PRC GAAP to non-distributable reserve funds, including a statutory surplus fund and a discretionary surplus fund. Each year, at least 10% of the after-tax-profit under PRC GAAP is required to be set aside as a statutory surplus fund until such appropriations for the fund equal 50% of the registered capital of the applicable entity. The appropriation for the discretionary surplus fund is at the Company's discretion as determined by the Board of Directors of each entity.



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Upon certain regulatory approvals and subject to certain limitations, the general reserve fund and the statutory surplus fund can be used to offset prior year losses, if any, and can be converted into paid-in capital of the applicable entity.

For the years ended December 31, 2011, 2012 and 2013, profit appropriation to the statutory surplus fund was approximately \$3.6 million, \$nil and \$16,000, respectively, and there was no profit appropriation to the general reserve fund for any of those years.

### 23. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted net income per share for the years indicated (in thousands except per share data):

	For the year ended December 31,		
	2011	2012	2013
<b>Numerator:</b>			
Net income attributable to Changyou.com Limited	\$245,456	\$282,400	\$268,642
Numerator for basic earnings per share	245,456	282,400	268,642
Numerator for diluted earnings per share	245,456	282,400	268,642
<b>Denominator:</b>			
Weighted average number of ordinary shares outstanding—basic	104,854	105,656	106,252
Incremental shares from treasury share method—restricted share units	1,746	1,136	424
Weighted average number of ordinary shares outstanding—diluted	106,600	106,792	106,676
Basic net income per share	\$ 2.34	\$ 2.67	\$ 2.53
Diluted net income per share	\$ 2.30	\$ 2.64	\$ 2.52

There were no potential ordinary shares that were anti-dilutive and excluded from the calculation of diluted net income per share for any of the years presented.





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## 24. SEGMENT INFORMATION

The Group has determined that it currently operates in the following principal reportable segments: (1) online game and (2) the 17173 Business. Others consists of cinema advertising only.

### Year Ended December 31, 2013 (in thousands)

	Online game	17173 Business	Others	Eliminations and adjustments	Consolidated
<b>Revenues(1):</b>					
Online game	669,168	—	—	—	669,168
Online advertising	—	54,882	—	(4,884)	49,998
IVAS	—	5,402	—	—	5,402
Others	—	—	25,031	(11,724)	13,307
<b>Total revenues</b>	<b>669,168</b>	<b>60,284</b>	<b>25,031</b>	<b>(16,608)</b>	<b>737,875</b>
<b>Cost of revenues:</b>					
Online game	93,048	—	—	187	93,235
Online advertising	—	13,797	—	—	13,797
IVAS	—	1,860	—	(74)	1,786
Others	—	—	17,518	—	17,518
SBC (2) in cost of revenues	71	30	—	—	101
<b>Total cost of revenues</b>	<b>93,119</b>	<b>15,687</b>	<b>17,518</b>	<b>113</b>	<b>126,437</b>
<b>Gross profit</b>	<b>576,049</b>	<b>44,597</b>	<b>7,513</b>	<b>(16,721)</b>	<b>611,438</b>
<b>Operating expenses:</b>					
Product development	109,964	9,470	—	—	119,434
Sales and marketing	122,452	14,722	7,143	(15,561)	128,756
General and administrative	52,622	3,375	570	—	56,567
Goodwill impairment and impairment of acquired intangibles via acquisition of businesses	—	—	—	—	—
SBC (2) in operating expenses	1,129	44	—	—	1,173
<b>Total operating expenses</b>	<b>286,167</b>	<b>27,611</b>	<b>7,713</b>	<b>(15,561)</b>	<b>305,930</b>
<b>Operating profit (loss)</b>	<b>289,882</b>	<b>16,986</b>	<b>(200)</b>	<b>(1,160)</b>	<b>305,508</b>
Interest income	28,419	23	13	—	28,455
Foreign currency exchange loss	(5,935)	—	(1)	—	(5,936)
Interest expense	(8,835)	—	—	—	(8,835)
Other income (expense)	3,187	(169)	113	482	3,613
<b>Income before income tax expense</b>	<b>306,718</b>	<b>16,840</b>	<b>(75)</b>	<b>(678)</b>	<b>322,805</b>
Income tax expense (credit)	35,988	(15)	410	—	36,383
<b>Net income</b>	<b>270,730</b>	<b>16,855</b>	<b>(485)</b>	<b>(678)</b>	<b>286,422</b>
Less: Net income attributable to the mezzanine classified non-controlling interest	17,780	—	—	—	17,780
<b>Net income attributable to Changyou.com Limited</b>	<b>252,950</b>	<b>16,855</b>	<b>(485)</b>	<b>(678)</b>	<b>268,642</b>



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**Year Ended December 31, 2012**  
**(in thousands)**

	Online game	17173 Business	Others	Eliminations and adjustments	Consolidated
<b>Revenues(1):</b>					
Online game	570,533	—	—	(187)	570,346
Online advertising	—	45,727	—	(3,202)	42,525
IVAS	—	4,307	—	—	4,307
Others	—	—	6,251	—	6,251
<b>Total revenues</b>	<b>570,533</b>	<b>50,034</b>	<b>6,251</b>	<b>(3,389)</b>	<b>623,429</b>
<b>Cost of revenues:</b>					
Online game	76,193	—	—	—	76,193
Online advertising	—	6,468	—	—	6,468
IVAS	—	1,696	—	(187)	1,509
Others	—	—	20,046	—	20,046
SBC (2) in cost of revenues	239	67	—	—	306
<b>Total cost of revenues</b>	<b>76,432</b>	<b>8,231</b>	<b>20,046</b>	<b>(187)</b>	<b>104,522</b>
<b>Gross profit</b>	<b>494,101</b>	<b>41,803</b>	<b>(13,795)</b>	<b>(3,202)</b>	<b>518,907</b>
<b>Operating expenses:</b>					
Product development	70,386	1,378	137	—	71,901
Sales and marketing	51,584	6,629	5,302	(3,202)	60,313
General and administrative	30,013	995	1,323	—	32,331
Goodwill impairment and impairment of acquired intangibles via acquisition of businesses	1,670	—	1,236	—	2,906
SBC (2) in operating expenses	3,258	105	—	—	3,363
<b>Total operating expenses</b>	<b>156,911</b>	<b>9,107</b>	<b>7,998</b>	<b>(3,202)</b>	<b>170,814</b>
<b>Operating profit (loss)</b>	<b>337,190</b>	<b>32,696</b>	<b>(21,793)</b>	<b>—</b>	<b>348,093</b>
Interest income	15,855	11	16	—	15,882
Foreign currency exchange loss	(558)	—	—	—	(558)
Interest expense	(2,243)	—	—	—	(2,243)
Other expense	(51)	—	(122)	—	(173)
<b>Income before income tax expense</b>	<b>350,193</b>	<b>32,707</b>	<b>(21,899)</b>	<b>—</b>	<b>361,001</b>
Income tax expense (credit)	67,748	—	(343)	—	67,405
<b>Net income</b>	<b>282,445</b>	<b>32,707</b>	<b>(21,556)</b>	<b>—</b>	<b>293,596</b>
Less: Net income attributable to the mezzanine classified non-controlling interest	11,196	—	—	—	11,196
<b>Net income attributable to Changyou.com Limited</b>	<b>271,249</b>	<b>32,707</b>	<b>(21,556)</b>	<b>—</b>	<b>282,400</b>



**Year Ended December 31, 2011**  
(in thousands)

	Online game	17173 Business	Others	Eliminations and adjustments	Consolidated
<b>Revenues(1)</b>	<b>\$435,512</b>	<b>\$44,981</b>	<b>\$ 10,853</b>	<b>\$ (6,770)</b>	<b>\$ 484,576</b>
Segment cost of revenues	49,735	3,764	13,783	—	67,282
SBC (2) in cost of revenues	102	128	—	—	230
<b>Total cost of revenues</b>	<b>49,837</b>	<b>3,892</b>	<b>13,783</b>	<b>—</b>	<b>67,512</b>
<b>Gross profit (loss)</b>	<b>385,675</b>	<b>41,089</b>	<b>(2,930)</b>	<b>(6,770)</b>	<b>417,064</b>
<b>Operating expenses:</b>					
Product development	47,234	2,139	466	—	49,839
Sales and marketing	48,241	2,015	5,447	(6,770)	48,933
General and administrative	23,149	2,394	1,613	—	27,156
Goodwill impairment and impairment of acquired intangibles via acquisition of businesses	—	—	5,420	—	5,420
SBC (2) in operating expenses	5,354	411	—	122	5,887
<b>Total operating expenses</b>	<b>123,978</b>	<b>6,959</b>	<b>12,946</b>	<b>(6,648)</b>	<b>137,235</b>
<b>Operating profit (loss)</b>	<b>261,697</b>	<b>34,130</b>	<b>(15,876)</b>	<b>(122)</b>	<b>279,829</b>
Interest income	11,916	—	17	—	11,933
Foreign currency exchange loss	(618)	—	—	—	(618)
Interest expense	(7)	—	—	—	(7)
Other income	267	2	188	—	457
<b>Income before income tax expense</b>	<b>273,255</b>	<b>34,132</b>	<b>(15,671)</b>	<b>(122)</b>	<b>291,594</b>
Income tax expense (credit)	40,965	2,732	(117)	—	43,580
<b>Net income</b>	<b>232,290</b>	<b>31,400</b>	<b>(15,554)</b>	<b>(122)</b>	<b>248,014</b>
Less: Net income attributable to the mezzanine classified non-controlling interest	2,558	—	—	—	2,558
<b>Net income attributable to Changyou.com Limited</b>	<b>\$229,732</b>	<b>\$31,400</b>	<b>\$ (15,554)</b>	<b>\$ (122)</b>	<b>\$ 245,456</b>

Note (1): The intercompany elimination for segment revenues mainly consists of sales and marketing services provided by the 17173 Business and the others business to the online game segment.

Note (2): "SBC" stands for share-based compensation expense.

As of December 31, 2013  
(in thousands)

	Online game	17173 Business	Others	Intercompany Eliminations	Consolidated
Cash and cash equivalents	\$ 535,659	\$ 6,882	\$ 5,943	\$ —	\$ 548,484
Restricted time deposits	424,674	—	—	—	424,674
Accounts receivable, net	21,477	10,926	3,593	—	35,996
Fixed assets, net	241,853	4,207	614	—	246,674
Intangible assets, net	47,776	3,820	21,799	—	73,395
Goodwill	154,095	26,157	—	—	180,252
<b>Total assets (1)</b>	<b>\$1,486,070</b>	<b>\$76,361</b>	<b>\$ 198</b>	<b>\$ 22,583</b>	<b>\$1,585,212</b>



As of December 31, 2012 (in thousands)					
	Online game	17173 Business	Others	Intercompany Eliminations	Consolidated
Cash and cash equivalents	\$ 360,377	\$ 2,449	\$ 3,813	\$ —	\$ 366,639
Restricted time deposits	246,599	—	—	—	246,599
Accounts receivable, net	14,558	7,617	1,189	—	23,364
Fixed assets, net	62,019	2,253	556	—	64,828
Intangible assets, net	29,575	188	24,486	—	54,249
Goodwill	116,992	17,929	—	—	134,921
<b>Total assets (1)</b>	<b>\$1,020,899</b>	<b>\$44,480</b>	<b>\$ 5,602</b>	<b>\$ 43,532</b>	<b>\$1,114,513</b>

Note (1): The intercompany elimination for segment assets mainly consists of an operating funds loan to and long term investment in the others.

## 25. TREASURY SHARES

On July 27, 2013, the Company's board of directors approved a share repurchase program (the "Share Repurchase Program"), pursuant to which the Company may repurchase from time to time at management's discretion, at prevailing market prices in the open market in accordance with Rule 10b-18 under the Securities Exchange Act of 1934, up to \$100 million of the Company's outstanding ADSs over a two-year period from July 27, 2013 to July 26, 2015. As of December 31, 2013, the Company had repurchased under the Share Repurchase Program an aggregate of 590,500 ADSs, representing 1,181,000 Class A ordinary shares at an average price of \$29.2 per ADS, or \$14.6 per Class A ordinary share, for aggregate consideration of \$17.24 million. These shares were recorded at their historical purchase cost of \$17.24 million and were not canceled.

## 26. RELATED PARTY TRANSACTIONS

The table below sets forth major related parties and their relationships with the Group.

<u>Company name</u>	<u>Relationship with the Group</u>
Sohu	Under common control of Sohu.com
Zhou You	An equity investee of the Company
Jin Dian	A controlled company by a member of board

On December 15, 2011, the Group completed the acquisition from Sohu of certain assets and business operations associated with the 17173 Business for fixed cash consideration of approximately \$162.5 million. Under the acquisition agreement, the net profit of \$1.3 million generated from the Group's operation of the 17173 Business during the Transition Period from December 16, 2011 through December 31, 2011, was for the benefit of Sohu. The Company accounted for this \$1.3 million as part of the consideration for the acquisition. See Note 6 "BUSINESS COMBINATIONS—Acquisition of the 17173 Business".

Jin Dian is controlled by Mr. Baoquan Zhang, who was a former member of our Board of Directors until his resignation on September 27, 2013. Jin Dian was no longer a related party of the Group after Mr. Zhang's resignation.



On November 29, 2011, the Group and Sohu separately entered into a services agreement and an online links and advertising agreement (together, the “Services and Advertising Agreements”), pursuant to which Sohu provide links and advertising space and technical support to the Group, including the provision and maintenance of user log-in, information management and virtual currency payment systems of the 17173 Business. The Services and Advertising Agreements provide for a term of twenty-five years for the virtual currency payment system services, and an initial term of three years for all the other relevant services and links and advertising space, and involve aggregate fees to Sohu of approximately \$30 million. Under the Services and Advertising Agreements, the Group may renew certain rights for a subsequent term of twenty-two years, and may obtain a perpetual software license in respect of the information management system and the user log-in system following the expiration of the three-year term, subject to the Group’s payment to Sohu of additional fees of up to approximately \$5 million in the aggregate. During the years ended December 31, 2011, 2012 and 2013, significant related party transactions were as follows:

	For the year ended December 31, (in thousands)		
	2011	2012	2013
<b>Transactions with Sohu</b>			
<i>Services provided by Sohu</i>			
Sales and marketing services provided by Sohu	\$ 6,002	\$14,026	\$13,390
Corporate expenses	1,483	27	12
Other service provided by Sohu	37	50	373
<i>Acquisition of the 17173 Business</i>			
Acquisition of the 17173 Business from Sohu	163,784	—	—
	For the year ended December 31, (in thousands)		
	2011	2012	2013
<b>Transactions with Jin Dian</b>			
Advertising slots provided by Shi Dai Jin Dian Cinema Investing Co., Ltd, or Jin Dian	\$ 763	\$ 1,552	\$ 1,310

As of December 31, 2012 and 2013, the amounts due to related parties were as follows:

	As of December 31, (in thousands)	
	2012	2013
Due to Jin Dian	\$ 4,191	\$ —
Due to Zhou You (royalty fees payable to Zhou You)	322	332

As of December 31, 2012 and 2013, amounts due from and prepayment to related parties were as follows:

	As of December 31, (in thousands)	
	2012	2013
Due from Sohu (mainly arising from customer advances collected by Sohu on behalf of the Group)	\$ 495	\$ 393
Short-term and long-term prepayments to Sohu under services and advertising agreements	20,239	10,363

The transactions are measured at the amount of consideration established and agreed to by the related parties, which approximates amounts charged to third parties. These balances are interest free and settleable on demand.



**27. COMMITMENTS AND CONTINGENCIES**

The Group has future rental commitments related to its bandwidth leasing charges, office rental, services and advertising agreements with Sohu, fees for game development services performed by third parties and purchase fees for in-progress online games developed by third-parties recorded in operating expenses and certain other services as follows:

	Bandwidth leasing (in thousands)	Office rental (in thousands)	Fees for game development services and in-progress games (in thousands)	Others (in thousands)
2014	\$ 7,578	\$ 9,607	\$ 6,498	\$ 396
2015	715	8,058	4,726	—
2016 and thereafter	127	18,840	13,412	—
<b>Total minimum payments required</b>	<b>\$ 8,420</b>	<b>\$ 36,505</b>	<b>\$ 24,636</b>	<b>\$ 396</b>

Rental expenses, including bandwidth leasing charges and office rental, were approximately \$17.7 million, \$23.1 million, and \$30.2 million, respectively, for the years ended December 31, 2011, 2012 and 2013 and were charged to the statement of comprehensive income as incurred.

The Group estimated the future capital commitments related to expenditures for games with technological feasibility and cinema advertising slot rights to be as follows:

	Expenditures for games with technological feasibility (in thousands)	Cinema advertising slot rights (in thousands)
2014	\$ 9,264	\$ 1,082
2015	4,550	8,931
2016 and thereafter	1,400	19,682
<b>Total minimum payments required</b>	<b>\$ 15,214</b>	<b>\$ 29,695</b>

The Group did not have any other significant capital and other commitments or guarantees as of December 31, 2013.

The Group did not have any material interest or penalties associated with tax positions nor did the Company have any significant unrecognized uncertain tax positions as of December 31, 2013.

The Group is not currently a party to any legal proceeding, investigation or claim which, in the opinion of the Group's management, is likely to have a material adverse effect on the business, financial condition or results of operations.

The Group has not recorded any legal contingencies as of December 31, 2013.

**28. RESTRICTED NET ASSETS**

Relevant PRC law and regulations permit payment of dividends by PRC-based operating entities, such as AmazGame, Gamease, Gamespace, Guanyou Gamespace, 7Road Technology, Shenzhen 7Road, Yan Fan Jing He, ICE Information, Shanghai ICE and Changyou RaidCall, only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. In addition, a PRC-based operating entity is required to annually appropriate 10% of net after-tax income to the statutory surplus reserve fund (see Note 22) prior to payment of any dividends, unless such reserve funds have reached 50% of the entity's registered capital. As a result of these and other restrictions under PRC law and regulations, PRC-based operating entities are restricted in their ability to transfer a portion of their net assets to the Company either in the form of dividends, loans or advances. Even though the Company currently does not require any such dividends, loans or advances from PRC-based operating entities for working capital and other funding purposes, the Company may in the future require additional cash resources from PRC-based operating entities due to changes in business conditions, to fund future acquisitions and development, or to declare and pay dividends to or distribution to its shareholders.

**29. SUBSEQUENT EVENTS**

On February 8, 2014, the Company's board of directors approved three new employee incentive plans, effective January 1, 2014, each with a term of 10 years, with payments to eligible employees under the plans to be based on adjusted net profits of the Group or adjusted net profits of certain specified projects. The Group will distribute an aggregate of up to 10% of the annual adjusted net profits of the Group and up to 20% of the adjusted net profits of the specified projects to eligible employees who participate in the plans.



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The Company has performed an evaluation of subsequent events through February 28, 2014, which is the date the financial statements were issued, with no other material events or transactions needing recognition or disclosure found.

### 30. ADDITIONAL INFORMATION—CONDENSED FINANCIAL STATEMENTS

The condensed financial statements of Changyou.com Limited have been prepared in accordance with SEC Regulation S-X Rule 5-04 and Rule 12-04.

The Company records its investments in subsidiaries under the equity method of accounting. Such investments and long-term loans to subsidiaries are presented on the balance sheet as “Interests in subsidiaries and variable interest entities” and the profit of the subsidiaries is presented as “Share of profit of subsidiaries and variable interest entities” in the statement of comprehensive income.

For the VIEs, where the Company is the primary beneficiary, the amount of the Company’s investment is included in the balance sheet as “Interests in subsidiaries and variable interest entities” and the profit or loss of the VIEs is included in “Share of profit of subsidiaries and variable interest entities” in the statement of comprehensive income.

The footnote disclosures contain supplemental information relating to the operations of the Company and, as such, these financial statements should be read in conjunction with the notes to the Consolidated Financial Statements of the Company. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted.

As of December 31, 2012 and 2013, there were no material contingencies, significant provisions for long-term obligations, or guarantees of the Company, except for those, if any, which have been separately disclosed in the consolidated financial statements.



### Financial information of Changyou.com Limited

#### Condensed Balance Sheets (In thousands, except par value)

	As of December 31,	
	2012	2013
	US\$	US\$
<b>Assets</b>		
<b>Current assets:</b>		
Cash and cash equivalents	10,674	17,579
Prepaid and other current assets	19	20
<b>Total current assets</b>	<b>10,693</b>	<b>17,599</b>
Interests in subsidiaries and variable interest entities	809,956	1,232,687
<b>Total assets</b>	<b>820,649</b>	<b>1,250,286</b>
<b>Liabilities and shareholders' equity</b>		
Short-term bank loans	113,000	353,331
Accrued liabilities	411	617
<b>Total current liabilities</b>	<b>113,411</b>	<b>353,948</b>
Long-term bank loans	99,353	—
<b>Total liabilities</b>	<b>212,764</b>	<b>353,948</b>
<b>Shareholders' equity</b>		
Class A ordinary shares par value \$0.01, 200,000 authorized; 21,494 and 23,184 issued and outstanding as of December 31, 2012 and 2013, respectively	215	244
Class B ordinary shares par value \$0.01, 97,740 authorized; 84,290 and 82,490 issued and outstanding as of December 31, 2012 and 2013, respectively	843	825
Additional paid-in capital	88,626	92,066
Treasury shares (nil and 1,181 shares, respectively as of December 31, 2012 and 2013)	—	(17,240)
Statutory reserves	9,351	9,367
Retained earnings	470,717	739,343
Accumulated other comprehensive income	38,133	71,733
<b>Total shareholders' equity</b>	<b>607,885</b>	<b>896,338</b>
<b>Total liabilities and shareholders' equity</b>	<b>820,649</b>	<b>1,250,286</b>

### Financial information of Changyou.com Limited

#### Condensed Statements of Comprehensive Income (In thousands)

	For the year ended December 31,		
	2011	2012	2013
	US\$	US\$	US\$
<b>Operating expenses:</b>			
General and administrative	1,969	3,195	3,552
<b>Total operating expenses</b>	<b>1,969</b>	<b>3,195</b>	<b>3,552</b>
<b>Operating loss</b>	<b>(1,969)</b>	<b>(3,195)</b>	<b>(3,552)</b>
Share of profit of subsidiaries and variable interest entities	247,399	287,251	283,436
Interest income (expense), net	26	(1,656)	(11,242)
<b>Income before income tax expense</b>	<b>245,456</b>	<b>282,400</b>	<b>268,642</b>
<b>Net income</b>	<b>245,456</b>	<b>282,400</b>	<b>268,642</b>
Other comprehensive income: Foreign currency translation adjustment	21,867	3,385	33,600
<b>Comprehensive income</b>	<b>267,323</b>	<b>285,785</b>	<b>302,242</b>



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**Condensed Statement of Cash Flows**  
**(In thousands)**

	For the year ended December 31,		
	2011 US\$	2012 US\$	2013 US\$
<b>Net cash used in operating activities</b>	<b>(1,937)</b>	<b>(4,893)</b>	<b>(14,668)</b>
<b>Cash flows from investing activities:</b>			
Shareholder loans to subsidiaries	(13,014)	(5,574)	(102,165)
<b>Net cash used in investing activities</b>	<b>(13,014)</b>	<b>(5,574)</b>	<b>(102,165)</b>
<b>Cash flows from financing activities:</b>			
Proceeds of loans from offshore banks	—	212,353	140,978
Dividend distributed to shareholders	—	(200,875)	—
Payment for repurchase of shares	—	—	(17,240)
<b>Net cash provided by financing activities</b>	<b>—</b>	<b>11,478</b>	<b>123,738</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>(14,951)</b>	<b>1,011</b>	<b>6,905</b>
<b>Cash and cash equivalents at beginning of year</b>	<b>24,614</b>	<b>9,663</b>	<b>10,674</b>
<b>Cash and cash equivalents at end of year</b>	<b>9,663</b>	<b>10,674</b>	<b>17,579</b>



Confidential Treatment Requested. Confidential portions of this document have been redacted and have been separately filed with the SEC.

Exhibit 4.78

Acquisition Framework Agreement

by and among

Beijing Gamease Age Digital Technology Co., Ltd.

CHANGYOU.COM WEBGAME (HK) LIMITED

Johnny, Cao Kai

Kent, Yang Zhiyi

Justin, Long Chunyan

Ben, Meng Shuqi

BURGEON MAX LIMITED

CADGWITH INVESTMENTS LIMITED

DOUBLE MERITS HOLDINGS LIMITED

EURO LOGISTICS LIMITED

7ROAD.COM LIMITED

Shenzhen 7Road Network Technology Co., Ltd

and

Shenzhen 7Road Technology Co., Ltd.

Relating to the equity interests in

7ROAD.COM LIMITED and Shenzhen 7Road Technology Co., Ltd.

Dated as of May 1, 2013





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### Acquisition Framework Agreement

This Acquisition Framework Agreement (“**Agreement**”) is entered into in Shenzhen City, the People’s Republic of China on May 1, 2013 by and among:

- (1) BURGEON MAX LIMITED (“**BVI-I**”), a limited liability company duly incorporated and validly existing under the laws of the British Virgin Islands, with its registered address at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands;
- (2) CADGWITH INVESTMENTS LIMITED (“**BVI-II**”), a limited liability company duly incorporated and validly existing under the laws of the British Virgin Islands, with its registered address at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands;
- (3) DOUBLE MERITS HOLDINGS LIMITED (“**BVI-III**”), a limited liability company duly incorporated and validly existing under the laws of the British Virgin Islands, with its registered address at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands;
- (4) EURO LOGISTICS LIMITED (“**BVI-IV**”), a limited liability company duly incorporated and validly existing under the laws of the British Virgin Islands, with its registered address at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Island (together with BVI-I, BVI-II and BVI-III, the “**Existing Shareholders of the Cayman Company**”);
- (5) Johnny, Cao Kai (曹凯), the sole shareholder of BVI-I, a Chinese citizen (ID card number: \* ), with his address at \*;
- (6) Kent, Yang Zhiyi (杨志毅), the sole shareholder of BVI-II, a Chinese citizen (ID card number: \* ), with his address at \*;
- (7) Justin, Long Chunyan (龙春燕), the sole shareholder of BVI-III, a Chinese citizen (ID card number: \* ), with his address at \*;
- (8) Ben, Meng Shuqi (孟书奇), the sole shareholder of BVI-IV, a Chinese citizen (ID card number: \* ), with his address at \* (Johnny, Cao Kai, Kent,

The symbol ‘\*’ in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.



Yang Zhiyi, Justin, Long Chunyan, Ben, Meng Shuqi shall hereinafter be collectively referred to as **“Existing Shareholders of the VIE Company”**; the Existing Shareholders of the VIE Company and the Existing Shareholders of the Cayman Company shall hereinafter be collectively referred to as the **“Sellers”**;

- (9) Beijing Gamease Age Digital Technology Co., Ltd., a limited liability company duly incorporated and validly existing under the laws of the People’s Republic of China, with its registered address at 2F, East Wing, Jingyan Hotel, No.29 Shi Jing Shan Road, Shi Jing Shan District, Beijing (**“Gamease Age”**);
- (10) Changyou.com Webgames (HK) Limited, a limited liability company duly incorporated and validly existing under the laws of Hong Kong, with its registered address at 304 Dominion Centre, 43 Queen’s Road East, Hong Kong (**“Gamease Hong Kong”**), and together with Gamease Age, the **“Purchasers”**;
- (11) 7Road.com Limited, a limited liability company duly incorporated and validly existing under the laws of Cayman, with its registered address at Scotia Centre, 4th Floor, P.O. Box 2804, George Town, Grand Cayman KY1-1112, Cayman Islands (the **“Cayman Company”**);
- (12) Shenzhen 7Road Network Technology Co., Ltd, a limited liability company duly incorporated and validly existing under the laws of the People’s Republic of China (the **“WFOE”**), with its registered address at 7F, Main Building, Matsunichi Peak Tower, No. 9996, Shennan Road, Nan Shan District, Shenzhen City; and
- (13) Shenzhen 7Road Technology Co., Ltd, a limited liability company duly incorporated and validly existing under the laws of the People’s Republic of China (the **“VIE Company”**), with its registered address at 8-9F, Main Building, Matsunichi Peak Tower, No. 9996, Shennan Road, Nan Shan District, Shenzhen City.

The foregoing are referred to as **Parties** collectively or a **Party** individually.

**WHEREAS:**

(1) Certain Parties hereto and Liqing Zeng, Yuan Wang, Tao Liu, Jie Zhang, Suzhou Green Pine Growth Partnership, Shenzhen Capital Group Co., Ltd entered into the Share Transfer Framework Agreement relating to the transfer of 68.258% equity interests in each of Shenzhen 7Road Technology Co., Ltd and its overseas Affiliate (“**Share Transfer Framework Agreement**”) on April 22, 2011, regarding the acquisition of 68.258% equity interests in the VIE Company by Gamease Age, the implement of the overseas reorganization plan of 7Road Group (defined as below) and the acquisition of 68.258% equity interests in the Cayman Company by Gamease Hong Kong (the “**Domestic and Overseas Share Transfer and Reorganization**”).

(2) The Domestic and Overseas Share Transfer and Reorganization has been completed before the date hereof. As of its establishment, the Cayman Company had issued 100,000 ordinary shares in total, which were, upon the completion of the overseas share transfer, held by the Existing Shareholders of the Cayman Company and Gamease Hong Kong respectively in accordance with the respective shareholding ratio of the Existing Shareholders of the VIE Company and Gamease Age in the VIE Company. Thereafter, Johnny, Cao Kai transferred 5,100 shares (5.1% of then all issued shares of the Cayman Company) through BVI-I back to the Cayman Company free of charge to be used for offering options and/or incentive shares under the employee share incentive plan of 7Road Group. After a share split, all the issued shares of the Cayman Company were changed to 100,000,000 ordinary shares and reclassified into 2 classes: (i) 94,900,000 Class B Ordinary Shares, held by the Existing Shareholders of the Cayman Company and Gamease Hong Kong respectively; and (ii) the 5.1% previously issued shares transferred by Johnny, Cao Kai to the Cayman Company free of charge were changed to 5,100,000 Class A Ordinary Shares after the shares split, which were reserved by the Cayman Company and of which restricted share units (“**RSUs**”) settleable upon vesting by the issuance of an aggregate of 2,546,250 shares have been granted to certain employees under the 2012 Share Incentive Plan of the Cayman Company. As of the date hereof, the shareholding structure of the Cayman Company is as follows:

Name	Amount of shares (Class B Ordinary Shares)	Shareholding
Gamease Hong Kong	68,258,000	71.926%
BVI-I	20,490,000	21.591%
BVI-II	2,090,000	2.202%
BVI-III	2,090,000	2.202%
BVI-IV	1,972,000	2.078%
Total	94,900,000	100.00%





(3) As of the date hereof, the shareholding structure of the VIE Company is as follows:

Name	Amount of capital contribution (RMB)	Shareholding
Gamease Age	6,825,800	68.258%
Johnny, Cao Kai	2,559,000	25.59%
Kent, Yang Zhiyi	209,000	2.09%
Justin, Long Chunyan	209,000	2.09%
Ben, Meng Shuqi	197,200	1.972%
Total	10,000,000	100.00%

The VIE Company, its shareholders and the WFOE have entered into a series of VIE Agreements (defined below), and the shares held by each shareholder of the VIE Company have been pledged to the WFOE based on the VIE Agreements.

(4) The Sellers intend to transfer all of their equity interests in the VIE Company and the Cayman Company (collectively referred to as the **“Target Shares”**) to the Purchasers in accordance with the terms and conditions hereof and to cease holding equity interests in 7Road Group entirely; the Purchasers agree to purchase the Target Shares.

To achieve the transaction goal in the foregoing and upon the consultation on the basis of equality, the Parties agree:

## I. Definitions and Interpretations

### 1.1 Definitions

In addition to the capitalised terms defined in the foregoing, unless otherwise provided in this Agreement, the following terms shall have the respective meanings set forth below:

<b>“Encumbrance”</b>	shall mean the mortgage, pledge, lien, right of first refusal, or any other third party rights and interests of any nature.
<b>“7Road Group”</b>	shall mean, collectively, the Cayman Company, 7Road.com HK Limited as the wholly-owned subsidiary of the Cayman Company, the WFOE and the VIE Company. Any provisions applicable to the 7Road Group shall be deemed to be applied to all members of the 7Road Group in the foregoing as a whole and individually.



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**“Shareholders Agreement of the VIE Company”**

shall mean the Shenzhen 7Road Technology Co., Ltd Shareholders Agreement signed by and among the Existing Shareholders of the VIE Company and Gamease Age on April 22, 2011.

**“VIE Agreements”**

shall mean a series of agreements and documents dated as of May 31, 2012 relating to the controlling power over the VIE Company, signed by and among the Existing Shareholders of the VIE Company, Gamease Age, the WFOE and the VIE Company (if applicable) pursuant to the Share Transfer Framework Agreement, including the Equity Interest Purchase Right Agreements, the Equity Interest Pledge Agreements, the Technology Development and Technology Utilization Service Agreement, the Spousal Consent Letters, the Business Operation Agreement, the Services and Maintenance Agreement, and the Intellectual Property Rights Transfer Agreement.

**“Shareholders Agreement of the Cayman Company”**

shall mean the Shareholders Agreement of 7Road.com Limited signed by and among the Existing Shareholders of the Cayman Company and Gamease Hong Kong on June 15, 2012.

**“Industrial and Commercial Administration”**

shall mean relevant industrial and commercial administrations in charge of the registration of companies and trademark registration.

**“Governmental Department”**

shall mean any government, quasi-government, any judicial, public, regulatory, legislative or statutory institution, any authority, entity, agency, ministry, bureau or unit or any arbitrator of the PRC or other jurisdictions, which has an authority on any Party in accordance with the law.



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<b>“Affiliates”</b>	shall mean, with respect to any Person, any other Person that controls, is controlled by or is under common control with such Person, directly or indirectly through one or more intermediaries. “Control” means the possession, direct or indirect, of the power to direct the management and policies of a Person, whether through ownership of voting securities, by contract or otherwise. If any Person, directly or indirectly, holds 50% or more of the equity interest of another Person, it shall be deemed as controlling such Person.
<b>“Business Day”</b>	shall mean a calendar day other than Saturday, Sunday or other legal holidays in the PRC.
<b>“Yuan”</b>	shall mean Renminbi Yuan, the lawful currency of the PRC.
<b>“China” or “PRC”</b>	shall mean the People’s Republic of China, solely for purposes of this Agreement, excluding Hong Kong Special Administrative Region, the Macau Special Administrative Region and Taiwan.
<b>“Material Adverse Change”</b>	shall mean any event, matter, situation, change, or development leading to or reasonably likely to cause Material Adverse Effects to the business, financial condition, operation and operational results of the 7Road Group, but changes of common economic or political factors are excluded.
<b>“Material Adverse Effect”</b>	shall mean any effect materially adverse to the business, assets, prospects, operation (including finance and other aspects), operational results or registered capital of an entity.
<b>“Person”</b>	shall mean natural person, partnership, corporation, limited liability company, joint stock company, trust, unincorporated enterprise, joint venture, governmental agency, or other institutions or organizations.



## 1.2 Interpretations

- (a) Unless otherwise provided, all references herein to Articles and Sections, shall be deemed to refer to Articles and Sections of or to this Agreement, as applicable.
- (b) The words “include,” “includes,” and “including” shall be deemed to be followed by “without limitation” or “but not limited to.”
- (c) References herein to one Party to this Agreement, other agreements, or documents shall include the successors or licensed assignees.

## II. Acquisition of the Target Shares

### 2.1 Acquisition Approach

Subject to the terms and conditions of this Agreement, the Sellers agree to transfer the Target Shares to the Purchasers at the price as provided in Section 2.2, and the Purchasers agree to purchase the Target Shares. Specifically:

- (a) Each of the Existing Shareholders of the Cayman Company will sell all of its equity interests in the Cayman Company to Gamease Hong Kong; and
- (b) Each of the Existing Shareholders of the VIE Company will sell all of his equity interest in the VIE Company to Gamease Age.

Each Seller hereby acknowledges that it consents to the sales by the other Sellers of their Target Shares, and irrevocably waives the right of first refusal and other similar preferential rights based on applicable law, articles of association of the VIE Company and/or the Cayman Company, Shareholders Agreement or any other organizational documents, regarding the Target Shares sold such other Sellers.

After the Closing (defined below) hereof, the Existing Shareholders of the VIE Company will no longer be parties to the VIE Agreements, since they no longer hold any equity interest in the VIE Company, and Gamease Age will continue performing the VIE Agreements as the sole shareholder of the VIE Company. The WFOE agrees to the transfer transaction under Section 2.1 (b), and for the purpose of the Closing hereof, agrees to remove the pledge on the equity interests in the VIE Company held by the Existing Shareholders of the VIE Company (including issuing necessary letters of approval regarding the removal of pledge and other documents as requested by the Industrial and Commercial Administration).



2.2 The Acquisition Consideration

- (a) The Parties agree that, after friendly consultation, subject to the terms and conditions hereof, the Purchasers shall pay \$78,010,052 (“**Acquisition Consideration**”) to the Sellers in total, regarding the acquisition of the Target Shares. Of the Acquisition Consideration, the Existing Shareholders of the Cayman Company shall receive \$46,268,052 (“**Overseas Consideration**”) as the consideration of the transfer of all their equity interests in the Cayman Company, and the Existing Shareholders of the VIE Company shall receive Renminbi equivalent to \$31,742,000 (“**Domestic Consideration**”) as the consideration of the transfer of all their equity interests in the VIE Company.  
  
The Parties confirm and agree that the aforesaid Domestic Consideration shall be paid to the Sellers in accordance with Section 2.3 of this Agreement by the Purchasers in Renminbi, at an exchange rate of 6.206 Yuan for 1 U.S. dollar.
- (b) The Parties confirm and agree that the Acquisition Consideration shall include the consideration for any and all undistributed profits of the 7Road Group associated with the Target Shares up to the Closing Day (defined as below). The Sellers may not further request to distribute any profits of the 7Road Group with respect to the Target Shares.
- (c) Regarding the amount of Acquisition Consideration provided in Section 2.2 of this Agreement, in the case that the Purchasers is required to withhold related tax from the Acquisition Consideration in accordance with applicable tax laws and regulations, the Purchasers may accordingly withhold such tax.





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## 2.3 Payment of The Acquisition Consideration

- (a) The Parties acknowledge and agree that, subject to terms and conditions of this Agreement, the Purchasers shall pay the Acquisition Consideration in cash to the following accounts designated, respectively, by the Sellers (“**Designated Accounts**”) after deducting any withholding tax (if applicable), in accordance with the allocation among the Sellers, the amounts of each installment payment and the timing of payment as follows:

			Time of payment/amount of payment by the Purchasers(\$)		
			The First Payment Day (as defined below)	The Closing Day (as defined below)	The Last Payment Day (as defined below)
The Sellers		The Acquisition Consideration (\$)			
The Existing Shareholders of the VIE Company	Johnny, Cao Kai	25,590,000	17,913,000	7,677,000	0
	Kent, Yang Zhiyi	2,090,000	1,463,000	627,000	0
	Justin, Long Chunyan	2,090,000	1,463,000	627,000	0
	Ben, Meng Shuqi	1,972,000	1,380,400	591,600	0
The Existing Shareholders of the Cayman Company	BVI-I	34,642,002	23,172,680	9,931,149	1,538,173
	BVI-II	3,949,682	2,654,951	1,137,836	156,895
	BVI-III	3,949,682	2,654,951	1,137,836	156,895
	BVI-IV	3,726,686	2,505,054	1,073,595	148,037

The Sellers  
 Johnny, Cao Kai  
 Kent, Yang Zhiyi  
 Justin, Long Chunyan  
 Ben, Meng Shuqi

The Designated Accounts  
 \*  
 \*  
 \*  
 \*

The symbol ‘ \* ’ in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.



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BVI-I Account Name: Burgeon Max Limited  
Bank of Deposit: \*  
Swift ID: \*  
Account Number: \*  
Bank Code: \*  
Message: \*

BVI-II Account Name: Cadgwith Investments Limited  
Bank of Deposit: \*  
Swift ID: \*  
Account Number: \*  
Bank Code: \*  
Message: \*

BVI-III Account Name: Double Merits Holdings Limited  
Bank of Deposit: \*  
Swift ID: \*  
Account Number: \*  
Bank Code: \*  
Message: \*

BVI-IV Account Name: Euro Logistics Limited  
Bank of Deposit: \*  
Swift ID: \*  
Account Number: \*  
Bank Code: \*  
Message: \*

- (b) The Sellers shall immediately issue and submit a written confirmation as formal receipt voucher to the Purchasers upon receiving each aforesaid payment.
- (c) Notwithstanding the foregoing, in the case that the Sellers are found to be in breach of their representations and warranties or obligations or covenants under this Agreement at any time, the Purchasers may claim against the Sellers for liabilities and indemnification pursuant to Article 9 of this Agreement.

#### 2.4 First Payment, Closing and Last Payment

- (a) The First Payment shall be paid to the Sellers at the first following Business Day after all the conditions precedent provided in Section 4.1(a) to 4.1(m) of Article 4 hereof have been satisfied or waived by the Purchasers in written form pursuant to Section 4.1 or other date agreed by the Purchasers and the Sellers ("**First Payment Day**") by the Purchasers in accordance with Section 2.3 of this Agreement. As conditions precedent of payment of First Payment, the Sellers shall designate a person with legitimate authorization of the Sellers, to issue and submit a confirmation letter to the Purchasers, which confirms that all the conditions precedent provided in Section 4.1(a) to 4.1(m) that the Sellers are responsible for have been satisfied or validly waived by the Purchasers, and provide the Purchasers with original copies/items of all related documents, certifications and items before the First Payment Day (no later than 1 Business Day before the First Payment Day).

The symbol ‘ \* ’ in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.



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- (b) The Closing shall take place at the time and the location agreed by Parties, on the first succeeding Business Day after all the conditions precedent of acquisition of the Target Shares provided in Article 4 hereof have been satisfied (or have been waived in written form by related Party who is permitted to waive pursuant to Section 4.1 and Section 4.2) or other date agreed by the Parties (“**Closing Day**”).

If the failure of occurrence of the Closing is attributed to any Party (e.g., failure to perform obligations under this Agreement leading to the failure to satisfy the conditions precedent which such Party is responsible for ), the Parties shall deal with it in the way provided in Article 11 of this Agreement.

Unless otherwise provided in the Domestic Separate Agreement or the Overseas Separate Agreement (as defined below), upon the Closing Day, the Purchasers and the Sellers shall designate a person respectively with their legitimate authorization, to issue and submit a confirmation letter to the opposite side, which confirms that all the conditions precedent provided in Section 4.1 (applicable to the Sellers) or Section 4.2 (applicable to the Purchasers) that the Parties are responsible for respectively have been satisfied as of the Closing Day (or waived by the opposite side), and provide the opposite side with original copies/items of all related documents, certifications and items (if such original copies/items shall be provided to the opposite side before the Closing Day pursuant to provisions of this Agreement, such provisions shall be observed).

- (c) From the Closing Day until the first anniversary date of the Closing Day, (i) if the Sellers do not breach any representation and warranty or any covenant or obligation under this Agreement, the Purchasers shall pay the Last Payment to the Sellers in accordance with Section 2.3 hereof on the fifth Business Day after the first anniversary date of the Closing Day or any other date agreed to by the Purchasers and the Sellers (“**Last Payment Day**”), (ii) if the Sellers breach any representation and warranty or any covenant or obligation under this Agreement, the Purchasers may choose not to pay the Last Payment and shall give a written notice to the Sellers not later than the fifth Business Day after the first anniversary date of the Closing Day. Nevertheless, the aforesaid arrangement related to the Last Payment shall not replace, terminate, exclude, and limit the Purchasers’ right to claim against the Sellers for responsibility of default in accordance with provisions hereof, regarding the Sellers’ breach of any representation and warranty or any obligation or covenant under this Agreement.



## 2.5 Separate Equity/Share Transfer Agreement

To consummate the transaction under this Agreement, the Parties agree to, (1) before Closing, duly execute and submit an Equity Transfer Agreement in the form of the VIE Company Equity Transfer Agreement attached hereto as Exhibit I (“**Domestic Separate Agreement**”), which will be used for submission to relevant Governmental Department and handling formalities and procedures required to transfer and register the equity in the VIE Company, and (2) before Closing, duly execute and submit a separate Share Transfer Agreement in the form of the Cayman Company Share Transfer Agreement attached hereto as Exhibit II (“**Overseas Separate Agreement**”), which will be used for handling formalities and procedures required to transfer the shares of the Cayman Company. For the avoidance of doubt, the Domestic Separate Agreement and the Overseas Separate Agreement shall be interpreted and applied together with this Agreement as a whole. Matters not included in the Domestic Separate Agreement and the Overseas Separate Agreement shall be implemented in accordance with this Agreement. Every related Party shall fully and duly perform his or its obligations under the Domestic Separate Agreement and the Overseas Separate Agreement, and any violation of such agreements shall be deemed as a violation under this Agreement. In the event of any conflict between the terms of the Domestic Separate Agreement or the Overseas Separate Agreement and this Agreement, the terms of this Agreement shall prevail.

## 2.6 Effects on Prior Agreements

Effective on the First Payment Day, (i) all agreements in Section 4.2 of the Share Transfer Framework Agreement shall be terminated, and the Sellers hereby unconditionally and irrevocably waive any original right, demand and claim under such Section; (ii) the non-compete obligations of the Sellers under the Share Transfer Framework Agreement, the Shareholders Agreement of the VIE Company, the Shareholders Agreement of the Cayman Company and the Labor Contracts and Non-compete Agreements between the Sellers and the VIE Company, shall be terminated, provided however, that the Sellers shall continuously observe Section 7.1(e) and 7.2(a) of this Agreement; (iii) the Shareholders Agreement of the VIE Company and the Shareholders Agreement of the Cayman Company shall be terminated. Notwithstanding the foregoing, such terminations shall not exclude or affect a Party’s right to claim against other parties for liabilities arising from such sections and other sections under aforesaid agreements.



### III. Tax, Costs and Expenses

The Sellers and Purchasers shall be responsible for their own taxes (including but not limited to enterprise income tax, personal income tax and stamp tax) and any related adverse consequences (if any) arising from the consummation of the transactions in this Agreement which are attributable to them according to applicable law. If the Sellers incur any economic losses to the 7Road Group, the Purchasers or their Affiliates due to any violation by the Sellers of any applicable laws such as failure to fulfill their related tax declaration or taxation payment obligations, the Sellers shall indemnify the 7Road Group, the Purchasers or the Affiliates of the Purchasers accordingly and all members of the Sellers shall bear joint liability.

In addition, the Sellers and the Purchasers shall assume their own costs and expenses paid or to be paid relating to the due diligence, preparation, negotiation and preparation of documents regarding the transactions of this Agreement, including engaging external lawyers, accountants, other professional consultants, negotiation and preparation of this Agreement and the completion of the transactions of this Agreement.

The Sellers and the Purchasers shall not incur any cost and expense to the 7Road Group due to execution and submission of this Agreement, performance of the obligations under this Agreement or preparation and implement of the transactions of this Agreement.

### IV. Conditions Precedent

#### 4.1 Conditions precedent for the Purchasers to agree on the Closing

The Purchasers' obligation to proceed with the Closing is subject to the fulfillment, , on or before the Closing Day (unless otherwise expressly agreed that certain conditions can only be satisfied on the Closing Day), of the conditions precedent provided under Section 4.1(a) through 4.1(o) (unless otherwise waived by the Purchasers in writing).

- (a) All representations and warranties made by the Sellers in Article 5 of this Agreement are true, correct and without any material omissions, as of the date of this Agreement and the Closing Day.





- (b) The Sellers have duly fulfilled all obligations and complied with all undertakings which shall be fulfilled and undertaken before the Closing Day, pursuant to this Agreement.
- (c) Shareholder meeting of the VIE Company has passed a resolution to approve the execution and performance of this Agreement as well as the consummation of the transaction of sale and acquisition of the equity interests in the VIE Company hereunder; and all of the Existing Shareholders of the VIE Company have voted for such meeting resolution.
- (d) The shareholders of the Cayman Company have passed a resolution to approve the execution and performance of this Agreement as well as the consummation of the transaction of sale and acquisition of the equity shares of the Cayman Company hereunder; and all of the Existing Shareholders of the Cayman Company have voted for such meeting resolution.
- (e) As of the date hereof, each of Johnny, Cao Kai, Kent, Yang Zhiyi, Justin, Long Chunyan has voluntarily and effectively resigned from any position in the 7Road Group including as a director, supervisor and senior manager; Ben, Meng Shuqi has voluntarily resigned as a director of any company of the 7Road Group as of the date of this Agreement. On the same day, the shareholders of each of the Cayman Company and the VIE Company have passed resolutions to elect the candidates, nominated by the Purchasers, to serve as the new directors, supervisors and senior managers of such company; and all of the Sellers have voted for such meeting resolutions.



- (f) After the date of this Agreement, the Sellers shall have used their best efforts to cooperate with the Purchasers to conduct the preliminary core technology test and accept the core assets after examination immediately, regarding all the business platforms of the 7Road Group, and have used their best efforts to assist the Purchasers in organizing related technology, business, financial, human resources, legal departments to test, accept after examination and check the business operation, enterprise management and condition of the assets of the 7Road Group and assist the Purchasers with the matters of relevant departments listed in Exhibit III hereto and accept after examination all the listed items, documents and materials. The Purchasers agree to complete the test and acceptance after examination provided in this section within 10 Business Days after the date hereof and the Sellers shall provide assistance. Unless otherwise proved that the Sellers haven't provided assistance in their best efforts, the expiration of the aforesaid duration is deemed as the fulfillment of the test, accept after examination and check obligations by the Sellers provided in this section
- (g) The Sellers have executed related Intellectual Property Rights Transfer Agreement with the VIE Company, pursuant to which the Sellers have unconditionally and irrevocably transferred all and any of their intellectual property rights related to the 7Road Group and its business or that may affect the business of the 7Road Group, to the VIE Company free of charge, whether or not the creation and improvement of such intellectual property rights are made independently or jointly, during working time or other time, at the place of business of the 7Road Group or other places. With regard to any transfers that require registration and/or approval of Governmental Department, the Sellers, together with related Parties, have submitted such transfer agreements and other related application materials to the competent intellectual property rights administration department for registration of such transfers, which applications have been formally accepted by such department.
- (h) Ben, Meng Shuqi has confirmed to stay in his post for a period of at least one year after the Closing Day.
- (i) No Governmental Departments or regulatory bodies of the PRC or any other jurisdictions have released, formulated or implemented any laws, regulations, rules, orders or notices prohibiting the transactions hereunder. No pending litigation, arbitration, dispute, investigation or any other pending legal proceedings or matters which prohibit or cause Material Adverse Changes to the transactions hereunder or cause the invalidity or unenforceability of this Agreement.
- (j) No material change has happened to the capital or ownership of the 7Road Group and no Material Adverse Change, bankruptcy, insolvency or failure to pay any due and payable debts have happened to the 7Road Group.
- (k) In the case that before the acquisition of shares in the VIE Company by Gamease Age, the removal of the pledge of equity shares in the VIE Company held by the Existing Shareholders of the VIE Company, or execution of any agreement or document by the WFOE and the Existing Shareholders of the VIE Company, are required by the Industrial and Commercial Administration, the Existing Shareholders of the VIE Company have finished the aforesaid work as requested by the Industrial and Commercial Administration.



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- (l) The Existing Shareholders of the Cayman Company have caused the Cayman Company to issue a Register of Members and a Register of Directors and Officers, both of which have been validly registered, certified and updated.
- (m) The Existing Shareholders of the VIE Company have caused the VIE Company to issue a Register of Members that the Gamease Age has been registered as the sole shareholder of the VIE Company. Moreover, the Existing Shareholders of the VIE Company and the VIE Company have submitted all necessary application documents with respect to the transaction of the transfer of shares in the VIE Company hereunder, the related changes of shareholders, directors, supervisors and senior managers of the VIE Company and the filing of any amendment of its articles of association, and such applications have been formally accepted. Applications for registration of any changes of directors, supervisors and senior managers of the WFOE have also been duly submitted to Industrial and Commercial Administration and such applications have been formally accepted.
- (n) The Existing Shareholders of the Cayman Company have caused the Cayman Company to issue a valid share certificate, which proves that all the issued shares of the Cayman Company are held by Gamease Hong Kong.
- (o) The Existing Shareholders of the VIE Company have caused and cooperated with the VIE Company to have successfully obtained the written notices issued by the Industrial and Commercial Administration to indicate its approval of the change of registration and filing, regarding the transaction of the transfer of shares in the VIE Company hereunder and the related changes of shareholders and amendment of the articles of association, and the VIE Company has been issued a new Business License (if required).



#### 4.2 Conditions precedent for the Sellers to agree on the Closing

The Sellers' obligations to sell the Target Shares to the Purchasers are subject to the fulfillment, on or before the Closing Day (unless otherwise waived by the Sellers in writing), of the conditions provided in following Section 4.2(a) to 4.2(c).

- (a) All representations and warranties made by the Purchasers in Article 6 of this Agreement are true, correct and without any material omissions, as of the date of this Agreement and the Closing Day.
- (b) The Purchasers have duly fulfilled all obligations and complied with all undertakings which shall be fulfilled and undertaken before the Closing Day pursuant to this Agreement.
- (c) No Governmental Departments or regulatory bodies of the PRC or any other jurisdictions have released, formulated or implemented any laws, regulations, rules, orders or notices prohibiting the transactions hereunder. No pending litigation, arbitration, dispute, investigation or any other pending legal proceedings or matters which prohibit or cause Material Adverse Changes to the transactions hereunder or cause the invalidity or unenforceability of this Agreement.

#### V. Representations and Warranties of The Sellers

The Sellers severally and jointly represent and warrant to the Purchasers that, on the date hereof and as of the Closing Day:

##### 5.1 Qualifications, powers and rights

- (a) If any of the Sellers is a company
  - (i) Such Seller is a legal person incorporated and effectively existing under the laws of the place of registration.
  - (ii) Such Seller has complete, exclusive, legitimate and effective rights and ownership of its Target Shares, free from any Encumbrance. Except for the Target Shares, such Seller does not hold any other shares/equity interests in the 7Road Group in any form or any rights convertible into any equity interests/shares in the 7Road Group (including but not limited to Restricted Share or RSUs settleable into Class A Ordinary Share in the Cayman Company).



(b) If any of the Sellers is a natural person

- (i) He/she is a PRC citizen with legitimate rights and capability to sign this Agreement and perform his or her obligations under this Agreement.
- (ii) He/she has complete, exclusive, legitimate and effective rights and ownership of his/her Target Shares from any Encumbrance (except the pledge under the VIE Agreements). Except for the Target Shares, such Seller does not hold any other shares/equity interests in the 7Road Group in any form or any rights convertible into equity interests/shares in the 7Road Group.

5.2 Authorization, validity of this Agreement

(a) If any of the Sellers is a company

- (i) Competent governing body of the Seller has officially held necessary meetings and approved this Agreement and the consummation of the transactions under this Agreement.
- (ii) The Seller has complete rights and authority to execute and deliver this Agreement and consummate the transactions under this Agreement. This Agreement has an effective binding force on the Seller once signed and delivered by the Seller.
- (iii) The execution, delivery and performance of this Agreement by the Seller and the consummation of the transactions hereunder or complying with the provisions of this Agreement will not (A) conflict with or cause violation of effective articles of association or similar organizational documents of such Seller or the 7Road Group; (B) cause or constitute violation to any agreement clauses, conditions or stipulations to which the Seller is a party; (C) violate any approval documents, orders, laws, regulations or rules applicable to the Seller, the 7Road Group or their respective properties or assets.

(b) If any of the Sellers is natural person

- (i) This Agreement has a lawful, effective binding force on the Seller once it is duly executed by the Seller.
- (ii) The execution and performance of this Agreement by the Seller will not violate or conflict with any applicable law, any agreement to which the Seller is a party or which has any binding effect on the property of the Seller, or any judgment, award, or decision by regulatory authorities.





### 5.3 Business and operation of the 7Road Group

- (a) The 7Road Group does not violate its articles of association and other corporate organizational documents or all the applicable PRC laws and regulations. There is no necessary government licenses, approvals, authorizations or permissions (collectively referred to as the **“Governmental Approvals”**) that have not been obtained in connection with the operation of the current important business of the 7Road Group and each of the Governmental Approvals remains completely effective. There is no pending or, to the knowledge of the Sellers, threatened legal proceedings that may cause any revocation, cancellation, suspension or revision to the Governmental Approvals.
- (b) The operation of business of the 7Road Group, especially the VIE Company is in good status, while the computer system and technology platform functions and maintains in normal conditions, where no material defects or hidden dangers exist.
- (c) All the joint operation agreements on the game research, development and operation between the 7Road Group and domestic game operation websites and the licensed operation agreements or joint operation agreements between the 7Road Group and overseas game operators have been properly and effectively executed. The 7Road Group complies strictly with such agreements and other agreements, contracts and other legal documents that may have material impacts on the current business and operation of the 7Road Group and has not breached any such agreements, contracts or legal documents.
- (d) The 7Road Group does not have the intention of investing abroad, co-investing with any third party, merging, acquiring, dividing or jointly operating with others, or signing any related documents; and there is no third party's right which affect and restrict the transactions provided in this Agreement.

### 5.4 Compliance

- (a) The 7Road Group has never committed any criminal offense, infringing activity or conducted any other behaviors violating any law and regulation or obligation where such behaviors relate to and have material impact on the 7Road Group or its business.



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- (b) The 7Road Group is under no negative government investigation or inquiry, and there is no factual basis that may lead to such investigation or inquiry.
- (c) There is not any failure of meeting any requirement of related Governmental Departments or any dispute with any Governmental Department, where such failure or dispute will cause Material Adverse Effect on the 7Road Group or its assets.

#### 5.5 Assets of the 7Road Group

- (a) Assets of the 7Road Group are not subject to eminent domain by any governmental authority or any plan for possessing or collecting all or part of such assets. The construction and location of any asset of the 7Road Group and the ownership or use of such assets and assets themselves have not violated any provision of any law and regulation or other legal requirements. All such assets owned or used by the 7Road Group have been properly maintained and repaired and can be used for the purpose for which such assets were designed, obtained and used, and are in good conditions as of this Agreement.
- (b) As to the real estates and movable properties (collectively referred to as the “**Properties**”) used in the operations of business, the 7Road Group has complete and transferable ownership or legitimate and effective leasehold rights, free from any rights and interests of any third party. There is no pending, or to the knowledge of the Sellers, threatened legal proceedings related to the Properties such as confiscation, forced transfer, freezing or other similar procedures.
- (c) The 7Road Group owns all necessary intellectual property rights for the operation of its current business (including but not limited to the whole game business operation), including but not limited to the legal right, the right of use through licenses or the right of use through other legal means of the confidential and/or proprietary information, trade secrets, trademarks, software copyrights and any other intellectual property rights. The Sellers do not own any other intellectual property rights in connection with the 7Road Group and its operation of business (registered or not), except for those to be transferred to the 7Road Group as defined above in Section 4.1(h). The intellectual property rights transferred by the Sellers to the 7Road Group in accordance with Section 4.1(h) are free from any pledge, mortgage, guarantee or any other rights of third party, and the foresaid transfer does not require any approval of or authorization from any third party.



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## 5.6 Information disclosure

The Sellers have provided the Purchasers the information and materials, as necessary to be disclosed based on their reasonable judgment, which is required to complete the transactions under this Agreement. The aforesaid information and materials do not contain any untrue statement of material facts and do not omit any statement of material facts.

## 5.7 Financial materials

Financial statements of the 7Road Group are prepared according to applicable U.S. GAAP, and fairly present the financial status, operation performance and cash flow of the 7Road Group, which are correct in all material aspects. Except for the debts disclosed in the financial statements, the 7Road Group has no other debts of any nature, including but not limited to: (i) any guaranty of any loan of others or similar obligations or responsibilities; and (ii) any financing services to any third parties (including its clients and affiliates), such as providing loans or reaching an agreement to assist such third parties in obtaining loans.

## 5.8 Labor and Managers

Directors, supervisors and senior managers of the 7Road Group nominated and/or appointed by the Sellers have performed their duties diligently, and are free from any incidence of violating their obligation to be honest and diligent toward the 7Road Group or impairing the benefits of the 7Road Group, as well as any obligation of directors, supervisors and senior managers under any applicable law and regulation; articles of association, shareholders agreement and other organizational documents of the members of the 7Road Group; any employment agreement and non-competition agreements signed by the aforesaid persons.

The WFOE and the VIE Company have not violated any current effective PRC law and regulation on social insurance and housing accumulation funds, including all the requirements on payments of social insurance and housing accumulation funds for employees; there is neither employment litigation or arbitration that may cause Material Adverse Effect on business, nor pending or threatened strikes and disputes with labor unions or other labor organizations.



Exhibit 4 of this Agreement provides a true, precise and complete name list of all key employees in the business operation and management of the 7Road Group, which does not omit any material information. The aforesaid employees (except Johnny, Cao Kai, Kent, Yang Zhiyi, Justin, Long Chunyan, whose employment will be terminated on the signing date of this Agreement as agreed to under this Agreement) properly remain in service and free from any dismissal or resignation. Exhibit 5 of this Agreement provides a true, precise and complete name list of all employees in-service of the 7Road Group as of January 1, 2013.

#### 5.9 Equity incentive plan for employees

There is no other official or unofficial equity incentive plan or shareholding plan that binds the 7Road Group or affects the current or future equity structure of the 7Road Group except for the equity incentive plan adopted by the Cayman Company in July, 2012 (“**2012 Share Incentive Plan**”). Incentive awards granted under the 2012 Share Incentive Plan have not been vested, and unless there is an IPO of the 7Road Group (as contemplated in the Share Transfer Framework Agreement), no Restricted Share or RSUs issued or granted under such incentive plan will be vested or have any possibility of being vested or settled..

#### 5.10 Tax

There are neither pending or threatened investigations or other similar tax related proceedings causing Material Adverse Effect on the 7Road Group, nor any violations of laws and regulations on tax by the 7Road Group. Each member of the 7Road Group declares and pays tax in accordance with laws and regulations and is free from any evasion or delay payment of tax or other violations of laws and regulations on tax.

#### 5.11 Litigation

There are no legal proceedings, arbitrations, disputes or other legal procedures which may cause significant losses to the 7Road Group or serious disturbances to the operation of its current business.

#### 5.12 Consents

No consent to the consummation of the transactions under this Agreement from any third party granted to the 7Road Group is necessary to be obtained,, including the consent under any loan contract, guarantee contract and other material contracts.



#### 5.13 Related party transactions

Terms and conditions in each related party transaction of the 7Road Group are not less favorable to the 7Road Group than those with independent third parties in similar transactions; and (i) the 7Road Group does not, directly or indirectly, owe any debt to its shareholders or their Affiliates; and (ii) no shareholder of the 7Road Group or their Affiliates owes any debt to the 7Road Group.

#### 5.14 No other agreements

Except for those referred to in this Agreement (including the Share Transfer Framework Agreement, the Shareholders Agreement of the VIE Company, the Shareholders Agreement of the Cayman Company, Labor Contracts and Non-compete Agreements between the Sellers and the VIE Company, the VIE Agreement), the Sellers and the 7Road Group have no other agreement or contract.

### VI. Representations and Warranties of the Purchasers

The Purchasers represent and warrant to the Sellers on the signing date of this Agreement, and as of the Closing Day:

#### 6.1 Qualifications

Each of the Purchasers is incorporated and effectively existing under applicable laws of its place of registration with a legal person status.

#### 6.2 Authorization, validity of this Agreement

The Purchasers have complete rights and authority to execute and deliver this Agreement and consummate the transactions under this Agreement. This Agreement, after duly execution and submission, constitutes legitimate, effective and binding obligations of the Purchasers in accordance with the terms hereof, and unless otherwise provided in applicable laws, it can be performed according to the terms of this Agreement.





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**6.3 Approval by competent authorization organs**

The competent governing bodies of the Purchasers have held relevant meetings and approved this Agreement and the transactions under this Agreement.

**6.4 No violations of laws and no defaults**

The execution, delivery and performance of this Agreement and the consummation of the transactions hereunder or complying with the provisions of this Agreement by the Purchasers will not (i) conflict with or cause violation of any provision provided in the respective effective articles of association of the Purchasers; (ii) cause violation of terms, conditions or stipulations of material agreements to which the Purchasers are parties; (iii) violate approval documents, governmental documents, orders, laws, regulations or rules applicable to the Purchasers or its any property or asset. Notwithstanding the foregoing, if violations and defaults under above (ii) and (iii) will not, individually or collectively, cause any Material Adverse Effect to the transactions hereunder, they will not be deemed as violations of this Section.

**6.5 Other Warranties**

The Purchasers have sufficient funding and capability to pay the Sellers for the Acquisition Consideration under this Agreement.

**VII. Covenants of the Sellers****7.1 Pre-Closing Covenants**

The Sellers covenant, severally and jointly, to the Purchasers that, as of the Closing Day, they shall:

- (a) ensure the fulfillment of the conditions precedent provided in Section 4.1, including but not limited to (i) taking necessary measures to ensure the execution and delivery of documents relating to the conditions precedent to which the Sellers are parties; (ii) Ben, Meng Shuqi having agreed to remain in his current position for at least one year from the Closing Day; (iii) ensuring that the important documents, materials, and items stipulated in Section 4.1 have been delivered before the Closing, and the arrangements for the Purchasers to accept the business and assets after examination before the Closing are properly made; and (iv) having made reasonable and necessary efforts to assist the Cayman Company and the VIE Company to complete the registrations of the transfers of the Target Shares, in accordance with applicable laws at the relevant registration authority and the department of industry and commerce administration, in order to complete the all registration and share transfer procedures of all the Target Shares transferred to the Purchasers hereunder;



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- (b) make best efforts to assist the 7Road Group to continue its business in the same manner as it did on or before the signing date of this Agreement in order to assist to avoid any changes detrimental to the operation and financial status of the 7Road Group; make commercially reasonable and necessary efforts to assist the 7Road Group to comply with applicable laws in all material aspects and to keep its business and its relations with clients, cooperators, creditors and employees in a regular way; and assist to maintain the stability of the assets of the 7Road Group;
- (c) unless for purposes of taking actions to effectuate this Agreement, to meet the need of the this Agreement or to conduct business operations, any acts or omissions procuring, causing and proposing the 7Road Group to conduct the following are prohibited (unless the Purchasers have already been aware of and approved such matters): (i) signing agreements or making commitments with value over RMB0.5 million Yuan; (ii) signing, revising, terminating any contract/commitment, or reaching any agreement or making any commitment, or borrowing money, or assuming any other debt; (iii) revising organizational documents and accounting policies of the 7Road Group (with the exception of revisions required by any law, provision or rule); (iv) providing any guaranty of any obligations of a third party, or signing any guarantee, compensation or other agreements to create any security interest over the assets or business of the 7Road Group; (v) increasing or decreasing the registered capital of the 7Road Group, or commencing any reorganization, bankruptcy or any procedure to terminate its business ; (vi) canceling, exempting, relieving or terminating its claims against any person, or concerning any pending litigation, arbitration and dispute, commencing any conciliation procedures; (vii) selling, leasing, licensing, transferring or disposing any asset (including but not limited to intellectual property rights) or changing any of its current business; or (viii) declaring or distributing any bonus or other distributions;
- (d) submit all documents or items to the Purchasers in a timely manner as required on and before the Closing Day under this Agreement; in order to meet the requirements under Section 4.1 regarding testing, acceptance after examination and inventory, the Sellers shall cause the technology, business, finance, human resource, legal and other relevant departments of the 7Road Group to prepare the items, documents and materials involved in the foresaid procedures for the acceptance after examination and handover;



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- (e) Johnny, Cao Kai, Kent, Yang Zhiyi, Justin, Long Chunyan and Ben, Meng Shuqi agree, on a joint and several basis, from the signing date of this Agreement until the second anniversary date of the Closing Day, without a prior written consent by the Purchasers, not to seek, allure, cause or permit, or assist others to seek, allure, cause or permit, or, in the activities supporting the foresaid matters, liaise with, any employee of the 7Road Group to terminate his employment with the 7Road Group. Johnny, Cao Kai, Kent, Yang Zhiyi, Justin, Long Chunyan and Ben, Meng Shuqi agree, on a joint and several basis, from the signing date of this Agreement until the second anniversary date of the Closing Day, in respect of the following employees of the 7Road Group: (a) all the in-service 7Road Group employees as of January 1, 2013 as listed in Exhibit 5; (b) all the employees employed by the 7Road Group after January 1, 2013; and (c) any key employee of the 7Road Group listed in Exhibit 4, without a prior written consent by the Purchasers, not to, nor procure any entity or individual which they control, directly or indirectly invest in or co-operate in any method (including being an owner, shareholder, partner, director, manager, adviser or consultant) to: (a) enroll, accept; or (b) assist others to enroll, accept, such employees, whether or not such employees will be accepted as employees, investors, shareholders, partners, directors, managers, advisers or consultants or in any other identities;
- (f) ensure that Ben, Meng Shuqi (after his resignation as a director but keeping his other positions) shall remain in his current positions for a period of at least 1 year after the Closing Day.
- (g) The Sellers make the reasonable best efforts to assist the Purchasers incompletely taking over the 7Road Group, and to assist the 7Road Group in achieving a smooth transition of its business operation and management.

## 7.2 Post-Closing Obligations

The Sellers covenant, on a joint and several basis, that after the Closing Day, they shall:

- (a) continue to perform the covenants provided in Section 7.1(e) and 7.1(g);
- (b) in respect of the intellectual property rights transfer matters provided in Section 4.1(h), if it is objectively impossible to complete the registration/ratification of the right-holder changes with intellectual property rights administration departments prior to the Closing Day, the efforts to complete such matters (including but not limited to possible requirements by government administration department and supplements of relevant materials) should continue after the Closing. The Sellers shall complete all foresaid registration/ratification procedures no later than six-month anniversary date of the Closing Day, to effectively transfer the intellectual property rights to the 7Road Group;



- (c) after the Closing Day, the Sellers shall comply with the requirement of Notice of the State Administration of Foreign Exchange on Relevant Issues concerning Foreign Exchange Administration for Domestic Residents to Engage in Financing and in Return Investment via Overseas Special Purpose Companies as well as the detailed rules for the implementation of such Notice, by filing applications for the cancellation of foreign exchange registration of abroad investment by the individuals with the Shenzhen Branch of the State Administration of Foreign Exchange as soon as possible since they no longer hold the shares of the Cayman Company. Such cancellation shall be completed no later than three months after the Closing Day, unless any delay of such cancellation was caused by reasons that cannot be ascribed to the Sellers, but under any event should such cancellation be completed no later than the six-month anniversary date of the Closing Day.

## VIII. Covenants of the Purchasers

### 8.1 Pre-Closing Covenants

- (a) Take necessary measures to ensure the signing and submission of documents relating to the conditions precedent to which they are parties;
- (b) Pay the Acquisition Consideration in accordance with this Agreement.

## IX. Default and Indemnifications

Unless otherwise provided in this Agreement, if a Party (referred to as the **“Breaching Party”**) fails to fulfill the obligations under this Agreement or makes untrue, inaccurate or misleading representations and warranties which violate this Agreement, such Breaching Party shall indemnify other non-breaching parties (referred to as the **“Non-Breaching Parties”**) for any expenses, losses, liabilities, damage compensation and reasonable expenditures incurred from such breaches, and:

- (a) if the foregoing breach is committed by more than one Party, each Breaching Party shall indemnify for the collective expenses, losses, responsibilities, damage compensations, disbursements and requests with other Breaching Parties on a joint and several basis;



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- (b) in respect of the indemnification responsibilities of any of the Sellers under this Agreement, the other Sellers have an obligation to bear them on a joint basis;
- (c) the Purchasers who delay the payment of Acquisition Consideration without good reasons shall pay an additional 0.05% of the account payable per day to compensate for breaching.

The amount of expenses, losses, liabilities, damage compensations and reasonable expenditures caused by any default of one Party to other Parties (referred to as the **"Amount of Loss"**) shall be determined according to the enforceable legal documents including judgment, arbitration award, verdict, ruling and decision of punishment relating to the default activities of the Breaching Party issued by competent court, arbitration authority, other dispute resolution organizations or governmental authorities. If the Amount of Loss cannot be identified through the foregoing way, then the Parties agree to settle the disputes according to the methods and procedures of resolution of disputes provided in Article 11.

The indemnification set forth in Section 9.1 (a) is additional, which shall not restrict other rights that may be acquired by Non-Breaching Parties according to this Agreement or current laws. The Parties acknowledge and agree that if any of the Parties fails to perform as provided in the specified articles of this Agreement, which may cause irreparable losses to the other Party, Non-Breaching Parties may not be adequately compensated solely by damages due to the breach of contract of any of the Parties. Therefore, besides any other legitimate rights and remedies, Non-Breaching Parties are entitled to enforce this Agreement through a verdict of substantial performance, and to obtain the temporary, preliminary and permanent injunctions in order to prevent any breach or potential breach of this Agreement by the other Party.



## X. Termination

### 10.1 Termination due to defaults

- (a) Unless otherwise provided in this Agreement, if any Party violates any material obligation under or provided by this Agreement, or makes any representation and warranty under or provided by this Agreement that are not true, not accurate, or misleading (considered as material violations of this Agreement) and does not rectify its violations within 15 days upon receiving written notification (or if such violations cannot be rectified, upon receiving the notification), any other Party, without prejudice to any other possible existing rights, may notify the other Parties in writing to terminate this Agreement before the Closing Day.
- (b) Any Party that terminates this Agreement according to Section 10.1 will not affect its rights to hold the Breaching Party liable according to provisions of Article 9 and laws.

### 10.2 Termination due to Material Adverse Changes and non-completion of conditions

Without prejudice to any other rights under this Agreement (including but not limited to any claims for the indemnifications of the Sellers for any default of their obligations), the Purchasers may notify the other Parties in writing to terminate this Agreement, if:

- (a) as of the 120th day after the signing date of this Agreement, any condition precedent still cannot be met and the Purchasers decide not to waive such unfulfilled condition precedent; or
- (b) if any Material Adverse Changes occur before the Closing Day, and within 30 days after the issuance of written notification indicating such Material Adverse Changes by the Purchasers to the other Parties, relevant Parties fail to reach any mutually acceptable solutions in writing.

### 10.3 Effect of Termination

If any Party terminates this Agreement pursuant to the terms of this Agreement, the Parties will be exempted from their respective obligations under this Agreement except for Article 5 (Representations and Warranties of the Sellers), Article 6 (Representations and Warranties of the Purchasers), Article 9 (Breach and Indemnity), Article 10 (Termination), Article 11 (Applicable Law and Resolution of Disputes), Section 12.2 (Notice), Section 12.3 (Confidentiality), Section 12.6 (Severability) and Section 12.7 (Non-waiving of rights). All above mentioned articles shall continue to be in full force and effect after the termination of this Agreement.





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## XI. Applicable Law and Resolution of Disputes

### 11.1 Applicable law

The effect, interpretations and performance of this Agreement shall be governed by the laws of the PRC.

### 11.2 Consultation

The Parties shall first settle any disputes relating to interpretations or fulfillment of this Agreement through friendly consultation.

### 11.3 Arbitration

If any dispute cannot be settled in a way acceptable to the relevant Parties within 60 days after the first consultation, such dispute shall be submitted to Shanghai International Economic and Trade Arbitration Commission which locates in Shanghai for final settlement. Arbitration shall be carried out according to then effective arbitration rules which are incorporated into herein by reference. Arbitration award shall be final and binding upon the relevant Parties.

## XII. Miscellaneous

### 12.1 Revision and amendment

According to applicable laws, any article of this Agreement can be revised, amended or supplemented in writing by the relevant Parties before the Closing Day (referred to as the **“Supplemental Agreement”**). If there are any conflicts between the Supplemental Agreement and this Agreement, the Supplemental Agreement shall prevail.

Unless provided otherwise in this Agreement, this Agreement does not exclude, limit or impact Parties' rights to hold other Parties liable for breaching the contract under other agreements such Parties made prior to this Agreement.



## 12.2 Notice

All notices and other communications under this Agreement shall be made in writing. If such are delivered to a Party by hand or sent by facsimile (must be confirmed), or sent by registered letter, or sent by express mail service (such as express postal service) to the address given for such Parties below (or such other address for such relevant Parties as shall be specified by like notice to the notifying Party), it shall be deemed delivered or made.

Johnny, Cao Kai

Address: \* ;

Tel.: \*

Zip code: 518000

E-mail: \*

Kent, Yang Zhiyi

Address: \* ;

Tel.: \*

Zip code: 518000

E-mail: \*

Justin, Long Chunyan

Address: \* ;

Tel.: \*

Zip code: 518000

E-mail: \*

Ben, Meng Shuqi

Address: \* ;

Tel.: \*

Zip code: 518000

E-mail: \*

BURGEON MAX LIMITED

Address: \* ;

Tel.: \*

Zip Code: 518000

E-mail: \*

**The symbol ‘ \* ’ in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.**



CADGWITH INVESTMENTS LIMITED

Address: \*;  
Tel.: \*  
Zip Code: 518000  
E-mail: \*

DOUBLE MERITS HOLDINGS LIMITED

Address: \*;  
Tel.: \*  
Zip code: 518000  
E-mail: \*

EURO LOGISTICS LIMITED

Address: \*;  
Tel.: \*  
Zip code: 518000  
E-mail: \*

Beijing Gamease Age Digital Technology Co., Ltd.

Address: 2F, East Wing, Jingyan Hotel, No. 29 Shi Jing Shan Road, Shi Jing Shan District, Beijing;  
Fax No.: 010- 68870371  
Tel.: \*  
Zip code: 100043  
E-mail: alex@cyou-inc.com

Changyou.com Webgames (HK) Limited

Address: 2F, East Wing, Jingyan Hotel, No. 29 Shi Jing Shan Road, Shi Jing Shan District, Beijing  
Fax No.: 010- 68870371  
Tel.: \*  
Zip code: 100043  
E-mail: alex@cyou-inc.com

The symbol ‘ \* ’ in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.



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**7Road. Com Limited**

Address: 7F, Main Building, Matsunichi Peak Tower, No. 9996, Shennan Road, Nan Shan District, Shenzhen City, Guangdong Province;

Tel.: 0755-61669777

Zip code: 518057

E-mail: tim.luo@7road.com

**Shenzhen 7Road Network Technology Co., Ltd.**

Address: 7F, Main Building, Matsunichi Peak Tower, No. 9996, Shennan Road, Nan Shan District, Shenzhen City, Guangdong Province;

Fax No.: 0755-86199356

Tel.: 0755-86199356

Zip code: 518057

**Shenzhen 7Road Technology Co., Ltd.**

Address: 8-9F, Main Building, Matsunichi Peak Tower, No. 9996, Shennan Road, Nan Shan District, Shenzhen City, Guangdong Province;

Fax No.: 0755-86199356

Tel.: 0755-86199356

Zip code: 518057

**12.3 Confidentiality**

The Sellers or any of its Affiliates shall keep confidential any nonpublic information related to the 7Road Group (including but not limited to the 7Road Group and its business, finance, products, technologies, staff, and other subject matters) as well as all information related to the existence of this Agreement (or any other transaction agreements) or the subject matters hereof or thereof (referred to as **“Confidential Information”**). Lacking of the Purchasers’ prior review and written consent, the Sellers or any of its Affiliates shall not release any information, notice and declaration, or communicate with any news media in respect of Confidential Information. The range of such review includes but not limited to the timing and content of the release or public declaration or communication of such news. The Sellers shall not slander, damage, injure and make any negative comments on the 7Road Group and the Purchasers in any media.

The Purchasers shall not slander, damage, injure and make any negative comments on the Sellers in any media.



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#### 12.4 Effectiveness

This Agreement becomes effective immediately upon its proper execution by the Parties.

#### 12.5 Counterparts

This Agreement is prepared in Chinese. This Agreement has 15 signed counterparts and each Party holds one. The remaining one counterpart is reserved to deliver to the competent industrial and commercial administration for alteration registration (if required). Each counterpart is with the same legal effect.

#### 12.6 Severability

If any article of this Agreement is found to be as invalid or unenforceable after the execution of this Agreement or becomes invalid or unenforceable due to any legislative changes, the remaining parts remain unaffected.

#### 12.7 Non-waiving of rights

Any Party failing to or delaying the exercise of any right or power under this Agreement shall not be deemed to waive such rights or powers. If any Party exercises any right or power independently or partially, it will not affect the exercise of such rights or powers in the future.

#### 12.8 Assignment

Any Party shall not transfer part of or all rights, interests, responsibilities or obligations under this Agreement in any method without prior written consent by the other Party.

[Signature Page Follows]



(This is the signature page of the Acquisition Framework Agreement relating to the equity interests in 7Road. com Limited and Shenzhen 7Road Technology Co., Ltd. This Agreement is signed by BURGEON MAX LIMITED, CADGWITH INVESTMENTS LIMITED, DOUBLE MERITS HOLDINGS LIMITED, EURO LOGISTICS LIMITED, Johnny, Cao Kai, Kent, Yang Zhiyi, Justin, Long Chunyan, Ben, Meng Shuqi, Beijing Gamease Age Digital Technology Co., Ltd., Changyou.com Webgames (HK) Limited, 7Road.com Limited, Shenzhen 7Road Network Technology Co., Ltd., as well as Shenzhen 7Road Technology Co., Ltd.)

BURGEON MAX LIMITED

Authorized representative: \_\_\_\_\_

Signed by: \_\_\_\_\_





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CADGWITH INVESTMENTS LIMITED

Authorized representative: \_\_\_\_\_

Signed by: \_\_\_\_\_



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DOUBLE MERITS HOLDINGS LIMITED

Authorized representative: \_\_\_\_\_

Signed by: \_\_\_\_\_



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EURO LOGISTICS LIMITED

Authorized representative: \_\_\_\_\_

Signed by: \_\_\_\_\_



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Johnny, Cao Kai

Signed by: \_\_\_\_\_



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Kent, Yang Zhiyi

Signed by: \_\_\_\_\_



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Justin, Long Chunyan

Signed by: \_\_\_\_\_





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Ben, Meng Shuqi

Signed by: \_\_\_\_\_



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Beijing Gamease Age Digital Technology Co., Ltd.

Legal representative:

Signed by: \_\_\_\_\_



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Changyou.com Webgames (HK) Limited

Authorized representative: \_\_\_\_\_

Signed by: \_\_\_\_\_



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7Road. com Limited

Authorized representative: \_\_\_\_\_

Signed by: \_\_\_\_\_



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Shenzhen 7Road Network Technology Co., Ltd.

Legal representative: \_\_\_\_\_

Signed by: \_\_\_\_\_



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Shenzhen 7Road Technology Co., Ltd.

Legal representative: \_\_\_\_\_

Signed by: \_\_\_\_\_





Exhibit I: Domestic Separate Agreement



Exhibit II: Overseas Separate Agreement



Exhibit III: List of Matters Required to Be Accepted after Examination



Exhibit IV: Name List of Key Employees



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Exhibit V: List of Employees In-Service on January 1, 2013



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**Exhibit 4.79****English Translation****Amended and Restated Equity Interest Purchase Right Agreement**

Among

**Shenzhen 7Road Network Technologies Co., Ltd.**

(As the Equity Interest Purchase Obligee)

**Beijing Gamease Age Digital Technology Co., Ltd.**

(As the Equity Interest Purchase Obligor)

And

**Shenzhen 7Road Technology Co., Ltd.**

June 5, 2013





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## AMENDED AND RESTATED EQUITY INTEREST PURCHASE RIGHT AGREEMENT

This Amended and Restated Equity Interest Purchase Right Agreement (hereinafter referred to as this “Agreement”) is entered into as of June 5, 2013 between and by the following Parties in Shenzhen, the People’s Republic of China (hereinafter referred to as “PRC”):

**Party A: Shenzhen 7Road Network Technologies Co., Ltd.**, with the registered address located at 7F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen and the legal representative is Wang Tao;

**Party B: Beijing Gamease Age Digital Technology Co., Ltd.**, with the registered address located at Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing; and the legal representative of Wang Tao;

**Party C: Shenzhen 7Road Technology Co., Ltd.**, with the registered address located at 8-9F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen and the legal representative is Wang Tao;

In this Agreement, all the above parties are called collectively as the “**Parties**” and respectively as a “**Party**”.

### WHEREAS:

1. Party A, a wholly foreign-owned enterprise incorporated under PRC laws;
2. Party C, a limited liability company incorporated under PRC laws and validly existing;
3. Party B, a limited liability company established according to the Chinese Law and the registered shareholders of Party C holding 100% equity interests of Party C (hereinafter referred to as “Equity Interests”);
4. A series of agreements and documents with respect to Party C’s right of control, including the Equity Interest Purchase Right Agreement, The Equity Interest Pledge Agreement, The Technology Development and Utilization Service Agreement, Spouse Consent, Power of Attorney, Business Operation Agreement, Services and Maintenance Agreement, Intellectual Property Transfer Agreement (hereinafter referred to as “VIE Agreements”) were entered into between and by Cao Kai, Yang Zhiyi, Long Chunyan, Meng Shuqi, original shareholders of Party C (“Original Shareholders”), Party B, Party A and Party C (if applicable) on June 26, 2012;
5. The Share Purchase Framework Agreement regarding Equity Interest of 7ROAD.COM LIMITED and Shenzhen 7Road Technology Co., Ltd. was entered among and by Party A, B and C, the Original Shareholders and other affiliated parties on May 1, 2013, and the Original Shareholders sold all shares in Party C to Party B. After the closing of the Framework Agreement, the Original Shareholders withdraw without holding any of Party C’s equity interest, and Party B, as the sole shareholder of Party C, continued to perform VIE Agreements;
6. The Amended and Restated Equity Pledge Agreement (hereinafter referred to as “Equity Pledge Agreement”) was entered by and between Party A and Party B on June 5, 2013;
7. The Amended and Restated Business Operation Agreement (hereinafter referred to as “Business Operation Agreement”) was entered among and by Party A, Party B and Party C on June 5, 2013;
8. The Parties intend to modify and restate the terms and conditions of Equity Interest Purchase Right Agreement executed on June 26, 2012 (hereinafter referred to as the “Original Equity Interest Purchase Right Agreement”) in accordance with the Agreement.



NOW, THEREFORE, through friendly negotiations, the Parties hereby agree to the followings:

# **1. Purchase Rights of Equity Interest**

## **1.1 Grant Rights**

Party B hereby exclusively, irrevocably and without any additional conditions grants to Party A or any or several designated person(s) (hereinafter referred to as "Designated Person") an option to purchase, at any time according to the steps determined by Party A, and at the price specified in Section 1.3 of this Agreement, from Party B a portion or all of the equity interests held by Party B in Party C (hereinafter referred to as the "Option"). No Option shall be granted to any third party other than Party A and/or the Designated Person. The "person" set forth in this Agreement means any individual person, corporation, joint venture, partnership, enterprise, trust or non-corporation organization.

## **1.2 Exercise Steps**

Party A and/or the Designated Person may exercise the Option by issuing a written notice (hereinafter referred to as the "Notice") in the form of the sample attached in Appendix to Party B specifying the specific percentage of equity interest to be purchased from Party B (hereinafter referred to as the "Purchased Equity Interest") and the manner of purchase.

Within 7 business days upon the receipt of the Notice, Party B shall enter into an equity transfer agreement with Party A and/or its designated person and ensure the transfer of Purchased Equity Interest to Party A and/or its designated person as soon as practicable.

## **1.3 Purchase Price**

1.3.1 When Party A exercises the Option, the purchase price of the Purchased Equity Interest (hereinafter referred to as "Purchase Price") shall be RMB 10,000. If the then applicable PRC laws permitted lowest price is higher than RMB 10,000, the Purchase Price shall be set at the lowest price permissible under the applicable laws.

1.3.2 Except for the Purchase Price provided under Clause 1.3.1, Party B shall not require Party A and/or the Designated Person to pay any other consideration.

## **1.4 Transfer of the Purchased Equity Interest**

After Party A provides written notice to purchase Equity Interest pursuant to this Agreement, each time the option is exercised:

1.4.1 Party B, as Party C's shareholder, shall make a shareholder's resolution for Party B to transfer the Equity Interest to Party A and/or the Designated Person;

1.4.2 Party B shall, pursuant to the terms and conditions of this Agreement and the Purchased Equity Interest Notices, enter into an equity interest transfer agreement with Party A and/or the Designated Person for each transfer;

1.4.3 The related parties shall execute all other requisite contracts, agreements or documents, obtain all requisite governmental approvals and consents, and conduct all necessary actions, without any security interest, transfer the valid ownership of the Purchased Equity Interest to Party A and/or the Designated Person, and have Party A and/or the Designated Person be the registered owner of the Purchased Equity Interest at administration for industry and commerce. In this clause and this Agreement, "Security Interest" includes guarantees, mortgages, pledges, the rights or interests of the third parties, any equity interest purchase right, right of acquisition, right of first refusal, right of set-off, ownership detainment or other security arrangements. It does not include any security interest subject to the Equity Pledge Agreement.

1.4.4 Party B and Party C shall unconditionally assist Party A in obtaining the governmental approvals, permits, registrations, filings and completing all necessary formalities for obtaining the Purchase Equity Interest.



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## 1.5 Payment

Payment method of the Purchase Price shall be determined through consultation by Party A and/or the Designated Person with Party B according to applicable laws when the Option is exercised.

**2. Party B and Party C's Promises**

- 2.1 Without the prior written consent of Party A, the Articles of Association of Party C shall not be supplemented, changed or amended in any form, Party C's registered capital shall not be increased or decreased, or the structure of Party C's registered capital shall not be changed in any other form.
- 2.2 Without the prior written consent of Party A, shall not sell, transfer, mortgage or dispose in any other form, any legitimate or beneficial Equity Interests, or approve any other security interest set on it except the pledges set on Party C's equity interests pursuant to the Equity Pledge Agreement.
- 2.3 Without the prior written consent of Party A, Party B, as Party C's shareholder, shall not make or execute any shareholders' resolution that approves any sale, transfer, mortgage or disposal of the legitimate or beneficial rights and interests of any Equity Interest, or allow any other security interest set on it, except pledges on the Equity Interests made to Party A or its Designated Person.
- 2.4 At any time, upon Party A's request, to immediately transfer Equity Interests to Party A and/or the Designated Person unconditionally at any time.
- 2.5 Without the prior written consent of Party A, Party B, as Party C's shareholder, shall not make or execute any shareholders' resolution that allows Party C to merge, associate with, acquire, or invest in any person.
- 2.6 According to good financial and business standards and customs, shall maintain the existence of Party C, prudently and effectively operate the business and handle affairs, ensure Party C's continuous and normal operation of all business to maintain the asset value of Party C, and refrain from any action/inaction which affects Party C's operations and asset value.
- 2.7 Without the prior written consent of Party A, shall not take any action and/or inaction, which may materially affect Party C's assets, business and liabilities; without the prior written consent of Party A, not sell, transfer, mortgage or dispose in any other form, any asset, legitimate or beneficial business interest or income of Party C, or approve any other security interest set on it at any time from the date of execution of this Agreement.
- 2.8 Without the prior written consent of Party A, Party C shall not enter into, inherit, guarantee or allow the existence of any debt, other than (i) debt arising in the ordinary course of business but not from borrowing; and (ii) debt already disclosed to and consented to in writing by Party A.



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- 2.9 Without the prior written consent of Party A, Party C shall not enter into any material contract, other than those in the ordinary course of business (As in this paragraph, any agreement that exceeding one hundred thousand Yuan (RMB 100,000.00) shall be deemed as a material contract).
- 2.10 Without the prior written consent of Party A, Party C shall not provide any loans or credit to anyone.
- 2.11 Upon the request of Party A, shall provide all operations and financial information of Party C.
- 2.12 Party C shall purchase and hold insurance from insurance companies accepted by Party A upon the request of Party A. The insurance amount and category shall be the same as those held by companies in the same area, operating a similar business and owning similar properties and assets as Party C.
- 2.13 Shall immediately notify Party A on the occurrence or the potential occurrence of any litigation, arbitration or administrative procedures related to the Equity Interests owned by Party B, or Party C's assets, business and revenue.
- 2.14 In order to keep the ownership of Party B's Equity Interest, shall execute all requisite or appropriate documents, conduct all requisite or appropriate actions, make all requisite or appropriate claim for rights, and take all requisite or appropriate defenses against claim reimbursement.
- 2.15 In order to keep ownership of Party C's assets, to execute all requisite or appropriate documents, conduct all requisite or appropriate actions, make all requisite or appropriate claim for rights, and take all requisite or appropriate defenses against claim reimbursement.
- 2.16 Without the prior written consent of Party A, Party C shall not distribute dividends to its shareholders in any manners.
- 2.17 Make any shareholder's resolution, as Party C's shareholder, in approval of the transfer of Purchased Equity Interests subject to this Agreement.
- 2.18 Upon the request of Party A, to appoint any persons designated by Party A as director or senior management personnel of Party C.
- 2.19 Party B shall exercise rights as Party C's shareholder upon the request, and only upon the written authorization of Party A.
- 2.20 To adhere strictly to the provisions of this Agreement and other Agreements entered into collectively or respectively by Party A, Party B and Party C, and to perform all obligations under these Agreements, without taking any action or inaction which affects the validity and enforceability of these Agreements.
- 2.21 If Party B receives a Purchase Price for its Equity Interests higher than RMB 10,000, or receive any form of profits distribution, dividend or bonus from Party C, Party B agrees that Party B shall waive the premium amount and any profit distribution, dividend or bonus (after deducting related taxes) as allowed by PRC laws, and Party A is entitled to these proceeds.



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**3. Party B and Party C's Representations and Warranties**

As of the execution date of this Agreement and every transfer date, Party B and Party C hereby represents and warrants to Party A as follows:

- 3.1 It has the right and ability to enter into and deliver on this Agreement and any equity interest transfer Agreements ("Transfer Agreement", respectively) which is a party of, for every transfer of Purchased Equity Interest pursuant to this Agreement, and to perform its obligations under this Agreement and any Transferring Agreement. Upon execution, this Agreement and the Transfer Agreements to which it is a party constitute a legal, valid and binding obligation enforceable against it in accordance with its terms;
- 3.2 The execution, delivery, and performance obligations of this Agreement and any Transfer Agreements shall not: (i) cause violation of any relevant PRC laws and regulations; (ii) constitute a conflict with its Articles of Association or other organizational documents; (iii) cause a breach to any Agreement or instrument which it is a party of or is bound by, or constitute a breach under any Agreement or instruments to which it is a party of or is bound by; (iv) cause violations of any relevant permits or approvals and (or) any relevant persistent valid conditions; or (v) cause any permits or approvals to be suspended, or revoked, or induce additional conditions;
- 3.3 Party C holds valid ownership and sales rights to all its assets. Party C has not set any security interest on these assets;
- 3.4 Party C does not have any unpaid debt, except (i) debt arising in the normal course business; and (ii) debt already disclosed to Party A to which Party A has approved in writing;
- 3.5 Party C complies with all PRC laws and regulations applicable to the acquisition of assets;
- 3.6 No litigation, arbitration or administrative procedure relevant to the equity interest and assets of Party C or the corporation is in process, pending settlement or likely to occur;
- 3.7 Party B holds valid ownership sales rights to its equity interest and has not any security interests on these interests, other than the security interests pursuant to the Equity Interest Pledge Agreement.

**4. Breach of Contract**

- 4.1 If any party (hereinafter referred to as "Defaulting Party") breaches any provision of this Agreement, which may cause damages to other parties (hereinafter referred to as "Non-defaulting Party"), the Non-defaulting Party can notify the Defaulting Party in writing, request rectification and correction of such a breach of contract; if the Defaulting Party does not take actions which rectify and correct such breach to the satisfaction of the Non-defaulting Party within fifteen (15) days upon the issuance of the written notice, the Non-defaulting Party can take actions pursuant to this Agreement or other measures in accordance with laws in response.
- 4.2 The occurrence of the following events constitutes a breach of contract by Party B:
  - (1) any violation by Party B of the provisions of this Agreement, or material mistakes, inaccuracies or other incorrect information in the representation and warranties hereunder;
  - (2) assignment or transfer in any manner of, or the pledging of, any rights pursuant to this Agreement without the prior written consent of Party A; or
  - (3) this Agreement and/or Equity Interest Pledge Agreement becomes invalid or unenforceable.





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- 4.3 Should a breach of contract or violation of provisions under the Equity Interest Pledge Agreement and/or Business Operation Agreement occur, Party A can request Party B to transfer to Party A or the Designated Person all or any percentage of the Purchased Equity Interests at the Purchase Price;
- 4.4 Once Party A realizes the pledge pursuant to Article 11 of the Equity Interest Pledge Agreement and, Party A obtains the relevant payments, Party B will be deemed to have fulfilled its obligations under this Agreement and Party A shall not request any other payments from Party B. and
- 4.5 Notwithstanding other provisions of this Agreement, the effect of Article 4 will not be affected by the termination of this Agreement.

## 5. Assignment

- 5.1 Without the prior written consent of the Party A, Party B shall not transfer its rights and obligations under this Agreement to any third party; if Party B is to be terminated, Party B agrees to transfer the rights and obligation under this Agreement to the person designated by Party A.
- 5.2 This Agreement shall be binding on Party B and the successor to Party B and is effective on Party A, any successor or Party A or transferee as allowed by Party A. Party B agrees, after his death to the extent permitted by law, Party A or the Designated Person will own the Party C's Equity Interests holding by him.
- 5.3 Party B hereby agrees that Party A shall be able to transfer all of its rights and obligation under this Agreement to any third party at its own discretion. Upon such transfer, Party A is only required to provide written notice to Party B, and no further consent from Party B will be required.

## 6. Effectiveness and Term

- 6.1 This Agreement shall be concluded and take effect as of the date of its execution; Once this Agreement takes effect, it shall supersede the Original Equity Interest Purchase Right Agreement executed by the Parties preceding the date of this Agreement.
- 6.2 The term of this Agreement is ten (10) years unless early termination in accordance with this Agreement or relevant provisions in any other relevant agreements reached by the Parties. This Agreement may be extended through the written confirmation by Party A before the expiration of this Agreement. The term of extension will be decided by Party A.
- 6.3 If Party A's or Party C's operation term expires (including any extensions of such term) or is otherwise terminated by any other reason prior to the expiration of this Agreement as set forth in Section 6.2, this Agreement shall be terminated upon such termination of such Party, except where Party A has transferred its rights and obligations in accordance with this Agreement.

## 7. Termination

- 7.1 At any time during the term of this Agreement, including any extension period, if Party A cannot exercise the Option indicated in Article 1 due to then applicable laws, Party A can, at its own discretion, unconditionally terminate this Agreement by issuing a written notice to Party B and does not need to assume any liability.
- 7.2 If Party C, during the term of this Agreement and its extension period, is terminated due to bankruptcy, dissolution or being ordered to close down by laws, the obligations of Party B hereunder are terminated upon the termination of Party C; Party B shall continue to perform its obligations under other agreements entered with Party A.
- 7.3 Except under circumstances indicated in Section 7.2, Party B and Party C does not have the right to terminate this Agreement during the term and extension periods of this Agreement.



## 8. Taxes and Expenses

Each Party shall, bear any and all taxes, costs and expenses as required by PRC laws for equity transfers incurred by or imposed on such Party arising from the preparation, execution and completion of this Agreement and all Transfer Agreements.

## 9. Confidentiality

- 9.1 The Parties acknowledge and confirm all oral or written materials exchanged by the Parties in connection with this Agreement are confidential. The Parties shall maintain the secrecy and confidentiality of these materials. Without the written consent of the other Parties, no Party shall disclose to any third party such materials, except under the following circumstances:
- (a) The materials are, or soon to be, public information (but disclosure cannot be done arbitrarily by the Party receiving the information);
  - (b) The materials are required to be disclosed under applicable laws or the rules or provisions of a stock exchange; or
  - (c) Where documents are disclosed by any party to its legal or financial counsel for the purpose of transactions described in this Agreement, the counsel shall also maintain confidentiality. Any disclosure by employees or agencies employed by any party shall be deemed as disclosure by such party and shall assume the liabilities for breach of contract pursuant to this Agreement.
- 9.2 Upon termination of this Agreement, one Party shall return all documents, materials or software containing confidential information upon the request of another Party, and cease to use such confidential information.
- 9.3 Notwithstanding other provisions of this Agreement, the effect of Article 9 will not be affected, no matter this Agreement is invalid, removed, terminated, or not operational for any reason.

## 10. Notices

Notices or other communications by any party relating to this Agreement shall be made in writing and delivered personally, sent by mail or by facsimile transmission to the addresses set forth below, or such other addressees specified by the relevant party from time to time. The effective date of the notice is determined as follows: (a) a notice delivered personally is deemed duly served upon delivery; (b) a notice sent by mail is deemed duly served on the seventh (7<sup>th</sup>) day after the date when the air registered mail with postage prepaid has been sent out (as is shown on the postmark), or the fourth (4<sup>th</sup>) day after it is delivered to an internationally recognized courier service; and (c) a notice sent by facsimile transmission is deemed duly served as of the receipt time shown on the transmission confirmation.

### Party A: Shenzhen 7Road Network Technologies Co., Ltd.

Legal Address: 7F, Matsunichi Hi-Tech Building, No. 9996, Shennan Boulevard, Nanshan District, 518057 Shenzhen

Contact: Chen Dwen

Fax: 0755-61669777 – 6



**Party B: Beijing Gamease Age Digital Technology Co., Ltd.**

Address: Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, 100043 Beijing

Contact: He Jie

Fax: 010-68870371

**Party C: Shenzhen 7Road Technology Co., Ltd.**

Legal Address: 8-9F, Matsunichi Hi-Tech Building, No. 9996, Shennan Boulevard, Nanshan District, 518057 Shenzhen

Contact: Chen Dewen

Fax 0755-61669777 – 6

**11. Applicable Law and Dispute Resolution**

- 11.1 The conclusion, validity, performance, modification, interpretation, termination and method of dispute resolution under this Agreement shall be governed by PRC laws.
- 11.2 The Parties shall strive to settle any dispute arising from the execution of this Agreement or disputes related to this Agreement through friendly negotiations.
- 11.3 If no settlement can be reached through negotiations within thirty (30) days after the request for consultation is made by any Party, either party can submit the matter to China International Economic and Trade Arbitration Commission with its then effective rules. The arbitration shall take place in Beijing. The arbitration decision shall be final and is binding upon the Parties. If there is a dispute or a dispute is in the process of arbitration, other than the matters in dispute, the Parties shall enjoy all other rights and perform all other obligations pursuant to this Agreement.

**12. Miscellaneous**

- 12.1 The headings contained in this Agreement are for convenient referencing only and do not affect the interpretation, explanation or meaning of the provisions of this Agreement.
- 12.2 The Parties confirm that upon this Agreement effectiveness, all Parties are in complete agreement respect to the subject matters and interpretations of this Agreement and replaces all prior verbal or/and written agreements and understandings (including but not limited to the Original Equity Interest Purchase Right Agreement).
- 12.3 This Agreement shall bind and benefit the Parties, the successors and the transferees allowed by each Party.
- 12.4 Any Party's failure to exercise or delay in exercising of any right and remedy (hereinafter referred to as "the Party's Rights") under this Agreement or laws shall not be deemed as a waiver of such rights, and shall not affect the future exercise of such rights in other manners or other the Party's rights by the same Party.
- 12.5 If any provision of this Agreement is judged as void, invalid or unenforceable under relevant laws, the provision shall be deemed invalid only within the applicable area of the law, The validity, legality and enforceability of the other provisions hereof are not affected or impaired in any way. The Parties shall cease performing such void, invalid or unenforceable provisions and replace these with provisions which are valid, effective and enforceable regarding to the specific facts and situation.



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- 12.6 The Parties agree the meaning of “Party A’s (prior) written consent” hereunder means approval by the board of Party A.
- 12.7 Any matters excluded in this Agreement shall be negotiated by the Parties. Any amendment or supplement to this Agreement shall be made in writing. Amendments and supplements duly executed by each Party shall be deemed as a part of this Agreement and enjoys the same legal effect as this Agreement.
- 12.8 This Agreement is made in three (3) original copies with each Party holding one (1) copy with the same legal effect.
- 12.9 The appendix hereto constitutes an integral part of this Agreement and has the same legal effect as this Agreement.

[No Text Below]



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(no text below, serving as Signature Page for the Amended and Restated Equity Interest Purchase Right Agreement executed by and among Shenzhen 7Road Network Technologies Co., Ltd., Beijing Gamease Age Digital Technology Co., Ltd. and Shenzhen 7Road Technology Co., Ltd. )

**Party A: Shenzhen 7Road Network Technologies Co., Ltd.**

Legal Representative: /s/ Wang Tao

**Party B: Beijing Gamease Age Digital Technology Co., Ltd.**

Signature: /s/ Wang Tao

**Party C: Shenzhen 7Road Technology Co., Ltd.**

Legal Representative: /s/ Wang Tao



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Appendix :

**Equity Purchase Notice**

To: Beijing Gamease Age Digital Technology Co., Ltd.

According to the Amended and Restated *Equity Interest Purchase Right Agreement* entered into between and by you and us dated June 5, 2013, we hereby notify and request you to transfer % equity interests in Shenzhen 7Road Technology Co., Ltd. to at a transfer price of RMB in accordance with the provisions of aforementioned agreement.

Regards,

**Shenzhen 7Road Network Technologies Co., Ltd.**

(Seal)

Date:





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**Exhibit 4.80**

**English Translation**

**Amended and Restated Equity Interest Pledge Agreement**

Among

**Shenzhen 7Road Network Technologies Co., Ltd.**

(As the Equity Interest Pledgee)

**Beijing Gamease Age Digital Technology Co., Ltd.**

(As the Equity Interest Pledgor)

And

**Shenzhen 7Road Technology Co., Ltd.**

June 5, 2013



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**CHANGYOU.COM LIMITED**

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## AMENDED AND RESTATED EQUITY INTEREST PLEDGE AGREEMENT

This Amended and Restated Equity Interest Pledge Agreement (hereinafter referred to as “this Agreement”) is entered into in Shenzhen, the People’s Republic of China (hereinafter referred to as “PRC” or “China”) on the day of June 5, 2013 by the following parties:

- (1) Shenzhen 7Road Network Technologies Co., Ltd., with the registered address located at 7F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen and the legal representative is Wang Tao (hereinafter referred to as “Pledgee”)
- (2) Beijing Gamease Age Digital Technology Co., Ltd., with the registered address located at Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing; and the legal representative is Wang Tao (hereinafter referred to as “Pledgor”)
- (3) Shenzhen 7Road Technology Co., Ltd., with the registered address located at 8-9F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen and the legal representative is Wang Tao.

(In this Agreement, all Parties are called collectively as the “Parties” and respectively as a “Party”).

### WHEREAS,

1. The Pledgee, a wholly foreign-owned enterprise duly incorporated and validly existing under the PRC laws;
2. Shenzhen 7Road Technology Co., Ltd. (hereinafter referred to as “7Road” or “the Company”), a limited liability company duly incorporated and validly existing under the PRC laws;
3. The Pledgor, a limited liability company established according to the Chinese law and the shareholder of the Company holding 100% equity interests of the Company;
4. A series of agreements and documents with respect to 7Road’s right of control, including The Equity Interest Purchase Right Agreement, The Equity Interest Pledge Agreement, The Technology Development and Utilization Services Agreement, Spouse Consent, Power of Attorney, Business Operation Agreement, Service and Maintenance Agreement and Intellectual Property Transfer Agreement (hereinafter referred to as “VIE Agreements”) were entered among and by Cao Kai, Yang Zhiyi, Long Chunyan, Meng Shuqi, original shareholders of 7Road (“Original Shareholders”), the Pledgor, the Pledgee and 7Road (if applicable) on June 26, 2012;
5. The Share Purchase Framework Agreement regarding Equity Interest of 7ROAD COM LIMITED and Shenzhen 7Road Technology Co., Ltd. (“Framework Agreement”) was entered among and by the Pledgor, the Pledgee, 7Road, the Original Shareholders and other affiliated parties on May 1, 2013, and the Original Shareholders sold all shares in 7Road to the Pledgee. After the closing of the Framework Agreement, the Original Shareholders withdraw from the VIE Agreements without holding any of 7Road’s equity interest, and the Pledgor, as the sole shareholder of 7Road, continued to perform the VIE Agreements;
6. The Pledgee and the Pledgor have entered into the Amended and Restated Equity Interest Purchase Right Agreement (hereinafter referred to as “Equity Interest Purchase Right Agreement”) dated June 5, 2013, according to which, the Pledgor shall transfer all or part of equity of 7Road it holds as required by the Pledgee and/or its designated entity or individual;
7. The Pledgee and 7Road have executed Technology Development and Utilization Services Agreement dated June 26, 2012 and Services and Maintenance Agreement dated June 26, 2012 (collectively referred to as “Services Agreements”), and 7Road shall pay service fee (hereinafter referred to as “Service Fee”) to the Pledgee under such agreements;



8. The Amended and Restated Business Operation Agreement (collectively referred to as “Main Agreements” together with Equity Interest Purchase Right Agreement and Services Agreements) was entered among and by the Pledgee, 7Road and the Pledgor on June 5, 2013;
9. In order to ensure that the Pledgor and the Company will perform their obligations under the Main Agreements, the Pledgor agrees to pledge all equity interests in the Company as the Pledgor’s and the Company’s security and Pledgee agrees to this pledge arrangement. Therefore, the Pledgee, the Pledgor and 7Road intend to amend and modify the Equity Interest Pledge Agreement (hereinafter referred to as “Original Equity Interest Pledge Agreement”) dated June 26, 2012.

**NOW, THEREFORE**, through friendly negotiations, the Parties hereby agree as follows:

## **1. Pledge and Guaranteed Scope**

- 1.1 The Pledgor agrees to pledge 100% of its equity interest in the Company to the Pledgee as a security for the Pledgor’s and the Company’s performance of obligations under the Main Agreements. The Company agrees that the Pledgor pledges its equity interest in the Company to the Pledgee pursuant to this Agreement. Rights of pledge hereunder refers to the rights owned by the Pledgee, who shall be entitled to a priority to be compensated by the proceeds from the conversion into money with a discount, auction or sale of the equity interest pledged by the Pledgor to the Pledgee.
- 1.2 The effect of guarantee under this Agreement shall not be affected due to the revision or modification of any of the Main Agreements and the guarantee to the obligations of the Pledgor and the Company under any revised Main Agreement shall keep effective. The invalid, withdrawal or termination of a Main Agreement shall not affect the validity of this Agreement. If the Main Agreement becomes invalid or is withdrawn or terminated, the Pledgee has the right to realize immediately the pledge in accordance with Article 11 of this Agreement.

## **2. Pledged Equity**

- 2.1 The pledged equity under this Agreement is 100% equity interests held by the Pledgor in the Company (hereinafter referred to as “Pledged Equity”) and all relevant interests. Upon the effectiveness of this Agreement, the situation of the Pledged Equity is set out below:  
 Company’s Name: Shenzhen 7Road Technology Co., Ltd.  
 Registered Capital: RMB10,000,000  
 Pledged Equity: 100% of equity interests of the Company  
 Capital Contribution corresponding to the Pledged Equity: RMB10,000,000
- 2.2 During the term of this Agreement, the Pledgee is not responsible for any dilution in value of the Pledged Equity unless he does so intentionally or with gross negligence having directly causal relationship with results, and the Pledgor has no rights to claim damage against the Pledgee in any manner or ask any requests.
- 2.3 Subject to Article 2.2 above, if the possibility of dilution in value of the Pledged Equity is significant enough to endanger the rights of the Pledgee, the Pledgee may at any time, on behalf of the Pledgor, to auction or sell the Pledged Equity, and negotiate with the Pledgor to have the proceeds from the auction or sale made as a prepayment for the guaranteed debt or have the proceeds deposited at a local Notary Public Office. (The Pledgee is responsible for all costs thus incurred.)



- 2.4 Whenever the Company or the Pledgor breaches this Agreement, the Pledgee is entitled to dispose the Pledged Equity in the manner set forth in Article 11.
- 2.5 The Pledgor can only increase its investment in the Company with the prior consent of the Pledgee. The increased capital investment in the Company due to such action of the Pledgor belongs to the Pledged Equity, and the Pledgor and the Pledgee shall enter into an Equity Interest Pledge Agreement to the satisfaction of the Pledgee for all equity interests held by the Pledgor in the Company pursuant to this Agreement.
- 2.6 The Pledgor gives up its rights to equity interest dividends during the effective term of the equity interest pledge.

### **3. Creation of Pledge**

- 3.1 The Pledgor undertakes that it shall be responsible for recording the pledge under this Agreement at the register of members of the Company on the date this Agreement is executed (hereinafter referred to as "Equity Pledged").
- 3.2 The Parties further agree that the Pledged Equity shall be recorded with the form attached hereto on the register of members of the Company and the certificate of investment, and the register of members and the certificate of investment shall be delivered to the Pledgee for keeping.
- 3.3 Whereas pledge shall be created after registering with the Administration for Industry and Commerce where the Company is registered. The Pledgor undertakes to register the pledge with the Administration for Industry and Commerce where the Company is registered, and the Company will try its best to cooperate with the Pledgor to complete such registration.

### **4. Term of Pledge**

- 4.1 The term of pledge pursuant to this Agreement shall start from the recording of the pledge at the Administration for Industry and Commerce where the Company is registered until the date that all obligations under Main Agreements have been performed (hereinafter referred to as "Pledge Term").
- 4.2 Within the Pledge Term, if the Pledgor and the Company have not performed or not appropriately performed the obligations under or incurred by the Main Agreements, the Pledgee has the right to exercise the pledge in accordance with Article 11 of this Agreement.

### **5. Keeping and Return of Pledge Certificate**

- 5.1 The Pledgor shall deliver the pledge certificate to the Pledgee within three (3) business days after the pledge is recorded on the register of members of the Company and is registered with the Administration for Industry and Commerce in accordance with Article 3; the Pledgee shall have such pledge documents well kept.
- 5.2 If the pledge hereunder is terminated pursuant to this Agreement, the Pledgee shall return the pledge certificate to the Pledgor within three (3) business days after the pledge is released pursuant to this Agreement and provide necessary assistance to the Pledgor for dealing with the process of the pledge's release.

### **6. Pledgor's Representations and Warranties**

The Pledgor hereby represents and warrants as of the execution date of this Agreement:

- 6.1 The Pledgor is the sole legal owner of the equity interest pledged.
- 6.2 The Pledgor has not set up any other pledges or other rights on the equity interest except that which is set for the Pledgee's benefit.



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- 6.3 The pledge under this Agreement constitutes the first order security interest of the Pledged Equity interests.
- 6.4 The Pledgor's shareholder meeting has approved the pledge pursuant to this Agreement.
- 6.5 Upon the effectiveness of this Agreement, this Agreement constitutes a legal, valid and binding obligation to the Pledgor.
- 6.6 The pledge pursuant to this Agreement by the Pledgor does not violate any relevant PRC laws and regulations and regulations of governmental departments or cause to breach any contracts or agreements with any third party or any promises made to any third party.
- 6.7 All relevant documents and materials related to this Agreement as provided by the Pledgor to the Pledgee are true, accurate and complete.

## 7. Representations and warranties of the Company

The Company hereby represents and warrants to the Pledgee that, until the effective date of this Agreement:

- 7.1 The Company is a limited liability company duly incorporated and validly existing under the PRC laws, and is an independent legal entity with complete status and capacity to sign, deliver and execute this Agreement and can be an independent litigation party.
- 7.2 All reports, documents and information provided by the Company to the Pledgee before the effectiveness of this Agreement regarding the Pledged Equity and upon requests of this Agreement are true and correct in all material respects.
- 7.3 All reports, documents and information provided by the Company to the Pledgee after the effectiveness of this Agreement regarding the Pledged Equity and upon requests of this Agreement are true and valid in all material respects.
- 7.4 This Agreement constitutes legal, effective and binding obligations to the Company after its signature.
- 7.5 The Company has complete rights and authorizations to sign and deliver this Agreement and all other documents related to all transactions under this Agreement and will be signed, as well as rights and authorizations to complete all transactions under this Agreement.
- 7.6 To the knowledge of the Company, there are no pending or threatening litigations, legal proceedings or claims against the Company or its assets (including but not limited to the Pledged Equity) at any courts, arbitration courts, government authorities or administrative authorities, which would have significant or adverse impact on the economic conditions of the Company or the Pledgor to perform obligations and the capability to guarantee liability under this Agreement.
- 7.7 The Company agrees to assume joint and several liabilities to the Pledgee for the representations and warranties of Article 6.1, 6.2, 6.3, 6.4 and 6.6 under this Agreement made by the Pledgor.
- 7.8 The Company warrants to the Pledgee that the above mentioned representations and warranties are true and correct, and have been fully complied with during all times before the agreement obligations have been fully performed or the secured debt has been completely paid off.





## 8. Pledgor's Promises

- 8.1 During the effective term of this Agreement, the Pledgor promises to the Pledgee for its benefit that the Pledgor shall:
- (1) complete the pledge registration at the Administration for Industry and Commerce immediately pursuant to this Agreement.
  - (2) not transfer or assign the equity interest, create or permit to create any pledges which may affect the rights or benefits of the Pledgee without the prior written consent of the Pledgee.
  - (3) comply with and implement relevant laws and regulations with respect to the pledge of rights; present to the Pledgee the notices, orders or suggestions with respect to the Pledge issued or made by the competent authority within five (5) days upon receiving such notices, orders or suggestions; and comply with such notices, orders or suggestions; or put forward objection and representations to the foregoing matters at the reasonable request of the Pledgee or with consent from the Pledgee.
  - (4) timely notify the Pledgee of any events or any received notices which may affect the Pledgor's equity interest or any part of its right, and any events or any received notices which may change the Pledgor's warranties and obligations under this Agreement or affect the Pledgor's performance of its obligations under this Agreement.
- 8.2 The Pledgor promises that the Pledgee's right to the pledge obtained from this Agreement shall not be suspended or inhibited by any legal procedure launched by the Pledgor or any successors of the Pledgor or any person authorized by the Pledgor or any such other person.
- 8.3 The Pledgor promises to the Pledgee that in order to protect or perfect the security for the performance of the Pledgor and the Company's obligations under the Main Agreements, the Pledgor shall execute in good faith and cause other interested persons relating to the right of pledge to execute all right certificates and contracts, and/or perform actions and cause other interested persons to take action, as required by the Pledgee; and provide convenience for the exercise of Pledged Equity and authorization by the Pledgee under this Agreement.
- 8.4 The Pledgor promises to the Pledgee that he will execute all amendment documents (if applicable and necessary) in connection with the certificate of Equity Interest with the Pledgee or its designated person (natural person or a legal entity), and provide all notices, orders and decisions it considered necessary related to the Pledge to the Pledgee within reasonable period.
- 8.5 The Pledgor promises to the Pledgee that he will comply with and perform all the warranties, commitments, covenants, representations and conditions for the benefit of the Pledgee. The Pledgor shall compensate all losses suffered by the Pledgee for the reason that the Pledgor fails to perform or fully perform its warranties, commitments, covenants, representations and conditions.
- 8.6 The Pledgor promises to adhere to the provisions of Business Operation Agreement, and exercise all rights as the Company's shareholder upon the request and only upon the written authorization of the Pledgee.

## 9. Promises of the Company

The Company promises the followings to the Pledgee for its benefit:

- 9.1 If signing and performing this Agreement and its pledge require any third party's agreement, permission, abstention, or authorization or any government agency's approval, permission or remission, or any registration or administration proceeding with any government agencies, the Company will try its best to satisfy and maintain such requirements during the term of this Agreement.



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- 9.2 Without the prior consent of the Pledgee, the Company will not assist or permit the Pledgor to create any new pledge or any other security interests on the Pledged Equity.
- 9.3 Without the prior written consent of the Pledgee, the Company will not assist or permit the Pledgor to transfer the Pledged Equity.
- 9.4 Whenever any litigation, arbitration or claim arises, and will adversely affect the Company, the Pledged Equity, or the interests of the Pledgee under the transaction agreement and this Agreement, the Company will immediately and promptly notify the Pledgee in writing, and will take all necessary actions to secure the Pledgee's right on the pledge upon the reasonable request of the Pledgee.
- 9.5 The Company will, during the first calendar month of every calendar quarter, provide the financial report of the immediately preceding calendar quarter, including but not limited to balance sheet, income statement and cash flow statement.
- 9.6 Upon the reasonable request of the Pledgee, the Company shall take all necessary actions and sign all necessary documents (including but not limited to the supplementary agreement to this Agreement) in order to ensure the exercise and realization of the Pledgee's rights on the Pledged Equity.
- 9.7 If executing the pledge right gives rise to any transfer of the pledge right, the Company shall take all necessary actions to complete such transfer.

## 10. Event of Default and Breach of Contract

- 10.1 The following events shall be regarded as an event of default:
- (1) Pledgor or the Company fails to perform the obligations under the Main Agreements;
  - (2) The Pledgor makes any material misleading or mistaken representations, warranties or covenants under Article 5, Article 6 and Article 8 herein; and the Pledgor breaches any other term and condition herein;
  - (3) The Pledgor waives the Pledged Equity or transfers or assigns the Pledged Equity without the written consent from the Pledgee;
  - (4) Any of the Pledgor's external loans, securities, compensations, covenants or any other compensation liabilities (i) are required to be repaid or performed prior to the scheduled date due to breach; or (ii) are due but cannot be repaid or performed as scheduled and thereby cause the Pledgee to believe that the Pledgor's capacity to perform the obligations herein is affected;
  - (5) The Company is incapable of repaying the general debt or other debt;
  - (6) This Agreement is illegal, invalid, or not workable or the Pledgor is not capable of continuing to perform the obligations herein due to any reason except force majeure;
  - (7) The property of the Pledgor is adversely changed causing the Pledgee to believe that the capability of the Pledgor to perform the obligations herein is affected;
  - (8) The Company performs partially or refuses to perform its obligations under the Main Agreements.
- 10.2 The Pledgor shall immediately give a written notice to the Pledgee if the Pledgor is aware of or finds that any event under Article 10.1 herein or any event that may result in the foregoing events has occurred.
- 10.3 Unless the event of default under Article 10.1 herein has been resolved to the Pledgee's satisfaction, the Pledgee, at any time when the event of default happens or thereafter, may give a written notice of default to the Pledgor and require the Pledgor to immediately perform the obligations under the Main Agreements or exercise the pledge right in accordance with Article 11 herein.
- 10.4 Notwithstanding other provisions of this Agreement, the effect of Article 10 will not be affected by the termination of this Agreement.



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**11. Exercise of the Pledge**

- 11.1 The Pledgor shall not transfer or assign the Pledged Equity without the written approval of the Pledgee prior to the completion of performing all the obligations under the Main Agreements.
- 11.2 In the event that an event of default as indicated in Article 10 occurs, the Pledgee shall give a notice of default to the Pledgor when the Pledgee exercises the right of pledge; the Pledgee may exercise the right of pledge at any time when the Pledgee gives a notice of default in accordance with Article 10.3 or thereafter.
- 11.3 The Pledgee is entitled to sale in accordance with legal procedures or disposition in other manners of the Pledged Equity. If the Pledgee decides to exercise its pledge rights, the Pledgor promises to transfer all of its shareholder's right to the Pledgee. In addition, the Pledgee has the right to convert the value of all or part of equity interests pursuant to this Agreement into money in compliance with legal procedures, or has priority of compensation from the proceeds generated from the auction or sale of all or a part of the equity interests under this Agreement.
- 11.4 The Pledgor shall not hinder the Pledgee from exercising the pledge right in accordance with this Agreement and shall provide necessary assistance so that the Pledgee could realize its pledge.

**12. Assignment**

- 12.1 The Pledgor shall not donate or transfer its rights and obligations herein without the prior written consent of the Pledgee. If the Pledgor is to be terminated, the Pledgor agrees to transfer the rights and obligation under this Agreement to the person designated by the Pledgee.
- 12.2 This Agreement shall be binding upon the Pledgor and its successors and be binding on the Pledgee and each of its successors and permitted assignees.
- 12.3 The Pledgee may transfer or assign its all or any rights and obligations under the Main Agreements to any individual designated by it (natural person or a legal entity) at any time to the extent permissible by the laws. In this case, the assignee shall enjoy and undertake the same rights and obligations herein of the Pledgee as if the assignee is a party hereto. When the Pledgee transfers or assigns the rights and obligations under the Main Agreements, and such transfer shall only be subject to a written notice serviced to the Pledgor, and at the request of the Pledgee, the Pledgor shall execute the relevant agreements and/or documents with respect to such transfer or assignment.
- 12.4 After the Pledgee's change resulting from the transfer or assignment, the new parties to the pledge shall execute a new pledge contract; and the content of new pledge contract shall accord with the content of this Agreement in all material aspects.

**13. Effectiveness and Termination**

- 13.1 The agreement is concluded upon its execution and takes effect on the date hereof; Once it takes effect, the Agreement shall supersede the Original Equity Interest Pledge Agreement executed by the Parties preceding to the Agreement.



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- 13.2 To the extent practicable, the Parties shall make their best efforts to register and put on record the pledge under the Agreement at the Administration for Industry and Commerce where the Company is located; but the Parties confirm that the effectiveness and validity of this Agreement shall not be affected whether the registration and records are completed or not.
- 13.3 The Pledgee shall cancel or terminate this Agreement after the Pledgor and/or the Company will not undertake any obligations under or incurred by the Main Agreements.
- 13.4 The release of pledge shall record accordingly at the register of shareholders of the Company, and complete the registration for removing the record at Administration for Industry and Commerce where the Company is located.

#### 14. Formalities Fees and Expenses

- 14.1 The Pledgor shall be responsible for all fees and actual expenses in relation to this Agreement including but not limited to taxes, legal fees, cost of production and any other charges. If the Pledgee pays the relevant taxes in accordance with laws, the Pledgor shall fully indemnify the Pledgee such taxes paid by the Pledgee.
- 14.2 The Pledgor shall be responsible for all reasonable fees incurred by the Pledgee from recourse actions by any means or ways for the reason that the Pledgor fails to pay any payable taxes, fees according to this Agreement.

#### 15. Force Majeure

- 15.1 Force Majeure, which includes but not limited to acts of governments, acts of nature, fire, explosion, geographic variation, typhoon, flood, earthquake, tide, lightning, war, riot, strike refers to any unforeseen events beyond a Party's reasonable control and cannot be foreseen and prevented with reasonable care. However, any shortage of credit, capital or financing shall not be regarded as an event beyond a Party's reasonable control. The effected Party by Force Majeure shall notify the other Party of such event.
- 15.2 In the event that the affected Party is delayed in or prevented from performing its obligations under this Agreement by Force Majeure, only within the scope of such delay or prevention, the affected Party will not be responsible for any damage by reason of such a failure or delay of performance. The affected Party shall take appropriate means to minimize or remove the effects of Force Majeure and attempt to resume performance of the obligations delayed or prevented by the event of Force Majeure. After the event of Force Majeure is removed, both Parties agree to resume the performance of this Agreement with their best efforts.

#### 16. Confidentiality

- 16.1 The Parties of this Agreement acknowledge and will ensure that all oral and written materials exchanged in connection with this Agreement are confidential. All Parties shall keep such materials confidential and cannot disclose them to any other third party without the other Parties' prior written approval, unless:
- (a) the public know and will know the materials (not because of the arbitrary disclosure by the Party receiving the information);
  - (b) the disclosed materials are required by laws or stock exchange rules; or
  - (c) materials relating to this transaction are disclosed to the Parties' legal consultants or financial advisors, however, who have to keep them confidential as well. Disclosure of the confidential by employees or hired institutions of the Parties is deemed as the act by the Parties, therefore, subjecting them to liability.
- 16.2 Notwithstanding other provisions of this Agreement, the effect of Article 16 will not be affected by the invalidity, dissolution and termination or non-enforcement of this Agreement for any reason.



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**17. Governing Law and Dispute Resolution**

- 17.1 The execution, validity, performance, amendment, interpretation and termination of this Agreement and the disputes resolution under this Agreement shall be governed by PRC laws.
- 17.2 The Parties shall strive to settle any dispute arising from or in relation to this Agreement through friendly negotiations.
- 17.3 In case no settlement can be reached through consultation within thirty (30) days after such dispute is raised, each Party can submit such matter to China International Economic and Trade Arbitration Commission in accordance with its then effective rules. The arbitration shall take place in Beijing. The arbitration award shall be final conclusive and binding upon both Parties. If any dispute is in the process of arbitration, other than the matters in dispute, the Parties shall perform the other rights and obligations pursuant to this Agreement.

**18. Notice**

Notices or other communications required to be given by any Party pursuant to this Agreement shall be made in writing and delivered personally or sent by mail or postage prepaid mail or by a recognized courier service or by facsimile transmission to the address of each Party or both Parties set forth below or other address of the Party or of the other addressees specified by such Party from time to time. The date when the notice is deemed to be duly served shall be determined as the follows: (a) a notice delivered personally is deemed duly served upon the delivery; (b) a notice sent by mail is deemed duly served the seventh (7<sup>th</sup>) day after the date when the air registered mail with postage prepaid has been sent out (as is shown on the postmark), or the fourth (4<sup>th</sup>) day after the delivery date to the internationally recognized courier service agency; and (c) a notice sent by facsimile transmission is deemed duly served upon the receipt time as is shown on the transmission confirmation of relevant documents.

**Pledgee: Shenzhen 7Road Network Technologies Co., Ltd.**

Address: 7F, Matsunichi Hi-Tech Building, No. 9996 Shennan Boulevard, Nanshan District, Shenzhen.  
Post code: 518057  
Contact: Chen Dewen  
Fax: 0755-61669777-6

**Pledgor: Beijing Gamease Age Digital Technology Co., Ltd.**

Address: Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing  
Post code: 100043  
Fax: 010-68870371

**Company: Shenzhen 7Road Technology Co., Ltd.**

Address: 8-9F, Matsunichi Hi-Tech Building, No. 9996 Shennan Boulevard, Nanshan District, Shenzhen.  
Post code: 518057  
Contact: Chen Dewen  
Fax: 0755-61669777-6



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**19. Miscellaneous**

- 19.1 The headings contained in this Agreement are for the convenience of reference only and shall not affect the interpretation, explanation or in any other way the meaning of the provisions of this Agreement.
- 19.2 The Parties confirm that this Agreement shall constitute the entire agreement of the Parties upon its effectiveness with respect to the subject matters therein and supersedes and replaces all prior or contemporaneous verbal or/and written agreements and understandings (including but not limited to the Original Equity Interest Pledge Agreement).
- 19.3 This Agreement shall be binding and benefit the successor of each Party and the transferee allowed by each Party.
- 19.4 Any Party's failure to exercise or delay in exercising of any right and remedy (hereinafter referred to as "the Party's rights") under this Agreement or laws shall not be deemed as a waiver of such rights, and shall not affect the future exercise of such rights in other manners or other the Party's rights by the same Party.
- 19.5 If any provision of this Agreement is judged by a competent court or a arbitration commission as void, invalid or non-enforceable according to relevant laws, and the validity, legality and enforceability of the other provisions hereof shall not be affected or impaired in any way. The Parties shall cease performing such void, invalid or non-enforceable provisions and replace those are void, invalid or non-enforceable provisions with valid provisions to the extent which such provisions could be valid, effective and enforceable.
- 19.6 The Parties agree and confirm that "the Pledgee's (prior) written consent" under this Agreement means approval by the board of the Pledgee.
- 19.7 Any matters excluded in this Agreement shall be negotiated by the Parties. Any amendment and supplement of this Agreement shall be made by the Parties in writing. The amendment and supplement duly executed by each Party shall be deemed as a part of this Agreement and shall have the same legal effect as this Agreement.
- 19.8 If this Agreement is re-executed or amended in respect of equity interest pledge required by relevant authorities for pledge registration, the Parties shall guarantee the effectiveness and enforcement of this Agreement.
- 19.9 This Agreement is made in five (5) original copies and each original copy has the same legal effect; Each Party holds one (1) original copy and others are for pledge registration at relevant authorities.
- 19.10 The appendix constitutes an integral part of this Agreement, and has the same legal effect.

(No text below)





[No text below, serving as Signature Page for the Amended and Restated Equity Interest Pledge Agreement]

**Pledgee: Shenzhen 7Road Network Technologies Co., Ltd.**

Legal Representative: /s/ Wang Tao

**Pledgor: Beijing Gamease Age Digital Technology Co., Ltd.**

Legal Representative: /s/ Wang Tao

**Company: Shenzhen 7Road Technology Co., Ltd.**

Legal Representative: /s/ Wang Tao



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**Register of Shareholders of Shenzhen 7Road Technology Co., Ltd.**

Date: June 5, 2013

Name/designation of shareholder	Contribution (RMB Yuan)	Holding ratio	Shareholder's information	Remarks:
Beijing Gamease Age Digital Technology Co., Ltd.	10,000,000	100%	Registered address: Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing Registered number: 110107010429510	Based on the Amended and Restated Equity Interest Pledge Agreement executed by and among Beijing Gamease Age Digital Technology Co., Ltd. (hereinafter referred to as "Gamease"), Shenzhen 7Road Network Technologies Co., Ltd. (hereinafter referred to as "7Road Network") and Shenzhen 7Road Technology Co., Ltd. (hereinafter referred to as "7Road Technology"), Gamease agrees to pledge its 100% equity interest in 7Road Technology to 7Road Network.

**Exhibit 4.81****English Translation****Power of Attorney**

The Company, Beijing Gamease Age Digital Technology Co., Ltd., a limited liability company legally established and validly existing in the People's Republic of China (hereinafter referred to as the "PRC"), is the shareholder of Shenzhen 7Road Technology Co., Ltd. (hereinafter referred to as "7Road Technology") holding 100% equity interest in 7Road Technology, hereby irrevocably authorizes the person ("Attorney-in-fact") designated from time to time by written resolution of the Board of Directors of Shenzhen 7Road Network Technologies Co., Ltd. (hereinafter referred to as "7Road Network") with the following powers and rights during the term of this Power of Attorney:

The Company hereby appoints the Attorney-in-fact as its exclusive and sole agent to exercise, on behalf of the Company, all shareholder's rights in accordance with PRC laws and 7Road Technology's Articles of Association (including the version currently in effect and the versions amended from time to time in future), including but not limited to making shareholders' resolutions (including matters such as nominating, electing, or appointing the director, general manager, principal financial officer or other senior management personnel, and determining distribution of dividend), to sell or transfer any or all of equity interests held by the Company in 7Road Technology.

Such authorization and appointment are based upon the precondition that the Attorney-in-fact is still serving in 7Road Network or its affiliates. Once the Attorney-in-fact loses his title or position in 7Road Network or its affiliates or the Board of Directors of 7Road Network terminates such authorization and appointment by written resolution and written notice, the authorization and appointment made by the Company hereby shall be no longer in force immediately and the new Attorney-in-fact nominated by written resolution of the Board of Directors of 7Road Network shall be authorized to exercise the full aforesaid rights on behalf of the Company.

The term of this Power of Attorney is equal to the term of the Amended and Restated Business Operation Agreement jointly executed by 7Road Technology, 7Road Network and the Company on June 5, 2013. If the term of the Amended and Restated Business Operation Agreement terminates prematurely or renews, the term of this Power of Attorney will terminate simultaneously or renew to the same term with the Amended and Restated Business Operation Agreement. Within the term of this Power of Attorney, this Power of Attorney shall not be revised or terminated without the written consent of 7Road Network.

Beijing Gamease Age Digital Technology Co., Ltd.

Authorized representative:

/s/ Wang Tao

June 5, 2013



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**Exhibit 4.82**

**English Translation**

**AMENDED AND RESTATED BUSINESS OPERATION AGREEMENT**

Among

**Shenzhen 7Road Network Technologies Co., Ltd.**

**Shenzhen 7Road Technology Co., Ltd.**

And

**Beijing Gamease Age Digital Technology Co., Ltd.**

June 5, 2013



## AMENDED AND RESTATED BUSINESS OPERATION AGREEMENT

This Amended and Restated Business Operation Agreement (hereinafter referred to as “this Agreement”) is entered into among the following parties in Shenzhen, the People’s Republic of China (hereinafter referred to as “China” or “PRC”) as of June 5, 2013:

- Party A:** **Shenzhen 7Road Network Technologies Co., Ltd.**, with the registered address located at 7F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen; and the legal representative is Wang Tao;
- Party B:** **Shenzhen 7Road Technology Co., Ltd.**, with the registered address located at 8-9F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen, China; and the legal representative is Wang Tao;
- Party C:** **Beijing Gamease Age Digital Technology Co., Ltd.**, with the registered address located at Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing; and the legal representative is Wang Tao;

(In this Agreement, all Parties are called collectively as the “Parties” and respectively as a “Party”.)

### WHEREAS,

1. Party A is a wholly foreign-owned enterprise duly incorporated under the PRC laws, which has technological expertise and practical experience with respect to the development and design of computer software, and rich experience and professional technicians with respect to information technology and services;
2. Party B is a limited liability company duly incorporated under the PRC laws, engaging in the development and operation of Web games;
3. Party C is a limited liability company duly incorporated under the PRC laws and the shareholder of Party B, holding 100% equity interest in Party B;
4. A series of agreements and documents, including Equity Interest Purchase Right Agreement, Equity Interest Pledge Agreement, Technology Development and Utilization Services Agreement, Spouse Consent, Power of Attorney, Business Operation Agreement, Service and Maintenance Agreement and Intellectual Property Transfer Agreement (hereinafter referred to as “VIE Agreements”) were entered among and by Cao Kai, Yang Zhiyi, Long Chunyan, Meng Shuqi, original shareholders of Party B (“Original Shareholders”), Party C, Party A and Party B (if applicable) on June 26, 2012.
5. The Share Purchase Framework Agreement regarding Equity Interest of 7ROAD COM LIMITED and Shenzhen 7th Road Technology Co., Ltd. (“Framework Agreement”) was entered among and by Party A, B and C, the Original Shareholders and other affiliated parties on May 1, 2013, and the Original Shareholders sold all shares in Party B to Party C. After the closing of the Framework Agreement, the Original Shareholders withdraw from the VIE Agreements without holding any of Party B’s equity interest, and Party C, as the sole shareholder of Party B, continued to perform the VIE Agreements.
6. Party A has established a business relationship with Party B by entering into an Technology Support and Utilization Service Agreement and Service and Maintenance Agreement (collectively, “Services Agreement”); Party B, pursuant to such agreements, is liable to pay a certain amount of money to Party A. Therefore, both parties are aware that the daily operation of Party B will have a material effect on its capacity to pay such payable account to Party A;
7. The Parties wish to further clarify matters relating to Party B’s operation via this Agreement. Now, the Parties intend to make amendment and restatement of the Business Operation Agreement dated June 26, 2012 (hereinafter referred to as “Original Business Operation Agreement”) in accordance with this Agreement.



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**NOW, THEREFORE**, through friendly negotiations, the Parties hereby agree as follows:

1. To assure the performance of the various operation agreements between Party A and Party B, including but not limited to the performance of the Services Agreement and the payment of the payable accounts by Party B to Party A, Party B together with Party C, as Party B's shareholder, hereby jointly agree that Party B shall not conduct any transaction which may materially affect its assets, obligations, rights or the company's operation without the prior written consent from Party A, including but not limited to the following contents:
  - 1.1 To enter into, inherit, guarantee or approve any debt, unless (i) incurred during the ordinary course of business other than through a loan debt; and (ii) debt disclosed to Party A and with the written consent of Party A.
  - 1.2 to enter into any material contracts, excluding contracts entered into during the ordinary course of business (for purpose of this clause, a contract value of more than one hundred thousand yuan (RMB100,000.00) shall be deemed a material contract);
  - 1.3 to sell any asserts or to confer on or assign any rights to any third party;
  - 1.4 to provide a loan or security in any manner to any third party;
  - 1.5 to assign to any third party its business agreements.
2. Party C, as Party B's shareholder, further covenants to Party A:
  - 2.1. not to sell, transfer, mortgage or dispose in any other manner of the legitimate or beneficial rights and interests of any equity interest, or to make any shareholders' resolution to approve such actions or to allow to create other security interests on it without Party A's written consent, except for Party A and/or its designated person;
  - 2.2. not to approve any shareholders' resolution which may result in Party B's merger or combination with, buying or investment in or being purchased by any other person (other than Party A or its designated person) without Party A's written consent;
  - 2.3. not to take any action/inaction that may materially affect the assets, business and liabilities of Party B without Party A's prior written consent; upon the execution of this Agreement, not to sale, transfer, mortgage or dispose, in any other form, any asset, legitimate or beneficial interest of Party B's business or income, or to approve any other security interest set on it without the prior written consent of Party A;
  - 2.4. in order to keep the ownership of Party B's equity interest, to execute all necessary or appropriate documents, take all necessary or appropriate actions, make all necessary or appropriate claims for right and defend against all claim reimbursement;
  - 2.5. not to request Party B to or approve any shareholder's resolution to distribute dividends or profits to the shareholders without Party A's written consent;
  - 2.6. not to supplement, amend or modify the articles of association of Party B, or to increase or decrease the registered capital of Party B, or to change the capital structure of Party B in any way without Party A's written consent;





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- 2.7. agree to execute the Power of Attorney attached hereto as requested by Party A upon the execution of this Agreement and within the term of this Agreement; and
- 2.8. excise his right as the shareholder of Party B only under the special written authorization of Party A and in accordance with the requirements of Party A.
3. In order to ensure the performance of the various operation agreements between Party A and Party B, including but not limited to the performance of the Services Agreement and the payment of the various payables by Party B to Party A, Party B together with Party C, as Party B's shareholder, hereby jointly agree to accept, from time to time, the corporate policy advice and guidance provided by Party A in connection with the employment and dismissal of the company's employees, daily operation, financial management and so forth.
4. Party B together with Party C hereby jointly agree that Party C, as Party B's shareholder, shall appoint the persons recommended by Party A as the directors of Party B, and Party B shall appoint Party A's senior managers as Party B's General Manager, principal financial officer, and other senior officers. If any of the above senior officers leaves or is dismissed by Party A, he or she will lose the qualification to take any position in Party B and Party B shall appoint other senior officers of Party A recommended by Party A to assume such positions. In such circumstance, the person recommended by Party A should comply with the stipulation on the statutory qualifications of directors, General Manager, principal financial officer, and other senior officers pursuant to applicable law.
5. Party B shall seek a guarantee from Party A first if it needs any guarantee for its performance of any contract or loan of working capital during the course of operation. In such case, Party A shall have the right but not the obligation to provide the appropriate guarantee to Party B at its own discretion. If Party A decides not to provide such guarantee, Party A shall issue a written notice to Party B in a timely manner and Party B shall seek a guarantee from a third party with the written consent from Party A.
6. Party A may at any time require Party B to assign the intellectual property owned by Party B to Party A and /or its designated person, the consideration of transfer should be subject to the negotiation of both Parties.
7. In the event that any of the agreements between Party A and Party B terminates or expires, Party A shall have the right but not the obligation to terminate all agreements between Party A and Party B including but not limited to the Services Agreement.
8. In the event that Party B and Party C fail to perform or to properly perform the obligation under this Agreement, such parties shall undertake joint liability for Party A's loss caused by their default.
9. Party B shall not assign its rights and obligations under this Agreement to any third party without the prior written consent of Party A; Party A may assign its rights and obligations under this Agreement as it needs and such transfer shall only be subject to a written notice sent to Party B by Party A, when any such transfer occurs, and no further consent from Party B will be required.
10. Each Party shall bear any and all taxes and costs incurred by or imposed on the Party in the preparation, execution of this Agreement and completion of transactions under this Agreement in accordance with PRC laws.



11. All Parties acknowledge and confirm that any oral or written materials communicated pursuant to this Agreement are confidential documents. All Parties shall keep secret of all such documents and not disclose any such documents to any third party without the prior written consent from the other parties unless under the following conditions: (a) such documents are known or shall be known by the public (excluding if the receiving party discloses such documents to the public without authorization); (b) any documents required to be disclosed in accordance with applicable laws or rules or regulations of stock exchange; or (c) if any documents required to be disclosed by any party to its legal counsel or financial consultant for the purpose of the transaction described in this Agreement, such legal counsel or financial consultant shall also comply with the confidentiality as stated hereof. Any disclosure by employees or agencies employed by any party shall be deemed the disclosure of such party and such party shall assume the liabilities for its breach of contract pursuant to this Agreement. This Article shall survive whether this Agreement is void, amended, canceled, terminated or unable to be performed.
12. Notices or other communications required to be given by any party pursuant to this Agreement shall be made in writing and delivered personally or sent by registered mail or postage prepaid mail or by a recognized courier service or by facsimile transmission to the address of each party or both parties as set forth below or other address of the party or of the other addressees specified by such party from time to time. The date when the notice is deemed to be duly served shall be determined as follows: (a) a notice delivered personally is deemed duly served upon the delivery; (b) a notice sent by mail is deemed duly served the seventh (7th) day after the date when the air registered mail with postage prepaid has been sent out (as is shown on the postmark), or the fourth (4th) day after the delivery date to the internationally recognized courier service agency; and (c) a notice sent by facsimile transmission is deemed duly served upon the receipt time as is shown on the transmission confirmation of relevant documents.

**Party A: Shenzhen 7Road Network Technologies Co., Ltd.**

Address: 7F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen.

Post Code: 518057

Contact: Chen Dewen

Fax: 0755-61669777-6

**Party B: Shenzhen 7Road Technology Co., Ltd.**

Address: 8-9F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen.

Post Code: 518057

Contact: Chen Dewen

Fax: 0755-61669777-6

**Party C: Beijing Gamease Age Digital Technology Co., Ltd.**

Address: 2F, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing.

Post Code: 100043

Contact: He Jie

Fax: 010-68870371

13. The conclusion, validity, performance, amendment, interpretation, termination and settlement of dispute of this Agreement shall be governed by the PRC laws.
14. The parties hereto shall in good faith strive to settle any dispute arising from the interpretation or performance of this Agreement. In the event the Parties cannot reach agreement within sixty (60) days after such dispute is raised, each party can submit such matter to China International Economic and Trade Arbitration Commission in accordance with its then effective rules. The arbitration shall take place in Beijing. The arbitration award shall be final conclusive and binding upon both parties. If any dispute is in process of arbitration, other than the matters in dispute, the Parties shall perform the other rights and obligations pursuant to this Agreement.



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15. This Agreement shall be executed by the Parties or a duly authorized representative of each Party as of the date first written above and become effective simultaneously; once taking effect, this Agreement shall supersede the Original Business Operation Agreement executed by the Parties preceding to this Agreement.
16. The Parties confirm that this Agreement shall constitute the entire agreement of the parties with respect to the subject matters therein and supersedes and replaces all prior or contemporaneous verbal and written agreements and understandings (including but not limited to the Original Business Operation Agreement).



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17. Any amendment and supplement of this Agreement shall be made in writing. The amendment and supplement duly executed by all parties shall be deemed as a part of this Agreement and shall have the same legal effect as this Agreement.
18. All provisions of this Agreement are severable. If any provision of this Agreement is judged as void, invalid or unenforceable, the validity, legality and enforceability of the other provisions hereof are not affected or impaired in any way.
19. This Agreement shall bind on and benefit the Parties, the successor and the transferees allowed by each Party.
20. The term of this agreement is ten (10) years unless early termination occurs in accordance with relevant provisions herein or in any other relevant agreements reached by all parties. This Agreement may be extended only upon Party A's written confirmation prior to the expiration of this Agreement and the extended term shall be determined by Party A at its sole discretion. During the aforesaid term, if Party A or Party B is terminated at expiration of the operation term (including any extension of such term) or by any other reason, this Agreement shall be terminated upon such termination of such party, unless such party has already assigned its rights and obligations in accordance with Article 9 hereof.
21. This Agreement shall be terminated on the expiration date unless it is renewed in accordance with the relevant provision herein. During the valid term of this Agreement, Party B shall not terminate this Agreement. Notwithstanding the above stipulation, Party A shall have the right but not the obligation to terminate this Agreement at any time by giving a thirty (30) days prior written notice to Party B.
22. The Parties agree and confirm the meaning of "Party A's (written) notice" pursuant to this Agreement means the consent shall be approved by the board of Party A.
23. This Agreement is made in three (3) originals with each party holding one (1) and all originals are equally valid.

**IN WITNESS THEREOF** each party hereto have caused this Agreement duly executed by itself or a duly authorized representative on its behalf as of the date first written above.

[No text below]



[No text below, serving as Signature Page for the Amended and Restated Business Operation Agreement]

**Party A: Shenzhen 7Road Network Technologies Co., Ltd.**

Legal Representative: /s/ Wang Tao

**Party B: Shenzhen 7Road Technology Co., Ltd.**

Legal Representative: /s/ Wang Tao

**Party C: Beijing Gamease Age Digital Technology Co., Ltd.**

Legal Representative: /s/ Wang Tao



**Appendix: Power of Attorney**

**Power of Attorney**

The company, Beijing Gamease Age Digital Technology Co., Ltd., a limited liability company legally established and validly existing in the People’s Republic of China (hereinafter referred to as the “PRC”), is the shareholder of Shenzhen 7Road Technology Co., Ltd. (hereinafter referred to as “7Road Technology”) holding 100% equity interest in 7Road Technology, hereby irrevocably authorizes the person (“Attorney-in-fact”) designated from time to time by written resolution of the Board of Directors of Shenzhen 7Road Network Technologies Co., Ltd. (hereinafter referred to as “7Road Network”) with the following powers and rights during the term of this Power of Attorney:

The Company hereby appoints the Attorney-in-fact as its exclusive and sole agent to exercise, on behalf of the Company, all shareholder’s rights in accordance with PRC laws and 7Road Technology’s Articles of Association (including the version currently in effect and the versions amended from time to time in future), including but not limited to making shareholders’ resolutions (including matters such as nominating, electing, or appointing the director, general manager, principal financial officer or other senior management personnel, and determining distribution of dividend), to sell or transfer any or all of equity interests held by the Company in 7 Road Technology.

Such authorization and appointment are based upon the precondition that the Attorney-in-fact is still serving in 7Road Network or its affiliates. Once the Attorney-in-fact loses his title or position in 7Road Network or its affiliates or the Board of Directors of 7Road Network terminates such authorization and appointment by written resolution and written notice, the authorization and appointment made by the Company hereby shall be no longer in force immediately and the new Attorney-in-fact nominated by written resolution of the Board of Directors of 7Road Network shall be authorized to exercise the full aforesaid rights on behalf of the Company.

The term of this Power of Attorney is equal to the term of the Amended and Restated Business Operation Agreement jointly executed by 7Road Technology, 7Road Network and the Company on June 5, 2013. If the term of the Amended and Restated Business Operation Agreement terminates prematurely or renews, the term of this Power of Attorney will terminate simultaneously or renew to the same term with the Amended and Restated Business Operation Agreement. Within the term of this Power of Attorney, this Power of Attorney shall not be revised or terminated without the written consent of 7Road Network.

Beijing Gamease Age Digital Technology Co., Ltd.

Authorized representative:

\_\_\_\_\_  
June 5, 2013





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**Exhibit 4.83**

**English Translation**

**Supplementary Agreement to Technology Development and Utilization Services Agreement**

Executed by

**Shenzhen 7Road Technology Co., Ltd.**

(As service receiver)

And

**Shenzhen 7Road Network Technologies Co., Ltd.**

(As service provider)

June 5, 2013



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**Supplementary Agreement to Technology Development and Utilization Services Agreement**

This Supplementary Agreement to Technology Development and Utilization Services Agreement (hereinafter referred to as the "Supplementary Agreement") is executed by the following two parties in Shenzhen, the People's Republic of China (hereinafter referred to as "China") on June 5, 2013:

- (1) Shenzhen 7Road Technology Co., Ltd., whose registered address is 8-9F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen, and legal representative of which is Wang Tao (hereinafter referred to as "Party A"); and
- (2) Shenzhen 7Road Network Technologies Co., Ltd., whose registered address is 7F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen, and legal representative of which is Wang Tao (hereinafter referred to as "Party B").

(In the Agreement, Party A and Party B are collectively referred to as the "Parties", respectively referred to as "Party" or "the other Party".)

**Whereas:**

The Parties executed the Technology Development and Utilization Services Agreement (hereinafter referred to as the "Original Agreement") on June 26, 2012, and Party B accepted Party A's entrustment to provide technology development and technology application services relating to online games to Party A.

Now, the Parties have agreed to make the following modifications to the terms concerning dispute settlement and notice in the Original Agreement upon consensus through negotiation:

**1 Dispute Settlement**

The Parties agree that Clause 14.3 in the Original Agreement shall be changed into: "If a party fails to settle any dispute through negotiation in sixty (60) days upon giving notice to the other party, then either party may submit such dispute to China International Economic and Trade Arbitration Commission for arbitration in Beijing based on then-current arbitration rules. Such award of arbitration is final and binding upon the Parties."

**2 Notice**

The Parties agree that the contact and fax number of the Parties under Clause 15 in the Original Agreement shall be changed into:

**Party A: Shenzhen 7Road Technology Co., Ltd.**

Contact: Chen Dewen

Fax: 0755-61669777 – 6

**Party B: Shenzhen 7Road Network Technologies Co., Ltd.**

Contact: Chen Dewen

Fax: 0755-61669777 – 6"



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In addition to the above modifications, the Parties have reached consensus upon the following terms:

- 1 Matters not contemplated herein shall be governed by relevant provisions in the Original Agreement; in case of conflict arising between the terms in the Original Agreement and those in the Supplementary Agreement, the latter shall prevail.
- 2 The Supplementary Agreement shall come into effect upon the date of signature and seal by the Parties.
- 3 The Supplementary Agreement is executed in four counterparts, and each party shall hold two copies. All counterparts have the same legal force and effect.

**Now, therefore,** the representatives, duly authorized by the Parties, have executed this Agreement as of the date first above written for mutual binding.

(The remainder of this page is intentionally left blank)



(Intended blank page, serving as signature page of the Supplementary Agreement to Technology Development and Utilization Services Agreement)

Party A: Shenzhen 7Road Technology Co., Ltd.

Legal representative: /s/Wang Tao

Party B: Shenzhen 7Road Network Technologies Co., Ltd.

Legal representative: /s/Wang Tao



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**Exhibit 4.84**

**English Translation**

**Supplementary Agreement to Services and Maintenance Agreement**

Executed by

**Shenzhen 7Road Technology Co., Ltd.**

(As service receiver)

And

**Shenzhen 7Road Network Technologies Co., Ltd.**

(As service provider)

June 5, 2013



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### Supplementary Agreement to Services and Maintenance Agreement

This Supplementary Agreement to Services and Maintenance Agreement (hereinafter referred to as the "Supplementary Agreement") is executed by the following two parties in Shenzhen, the People's Republic of China (hereinafter referred to as "China") on June 5, 2013:

- (1) **Shenzhen 7Road Technology Co., Ltd.**, whose registered address is 8-9F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen, and legal representative of which is Wang Tao (hereinafter referred to as "Party A"); and
- (2) **Shenzhen 7Road Network Technologies Co., Ltd.**, whose registered address is 7F, Matsunichi Hi-Tech Building, 9996 Shennan Boulevard, Nanshan District, Shenzhen, and legal representative of which is Wang Tao (hereinafter referred to as "Party B").

(In the Agreement, Party A and Party B are collectively referred to as the "Parties", respectively referred to as a "Party" or "the other Party".)

#### Whereas:

The Parties executed the Services and Maintenance Agreement (hereinafter referred to as the "Original Agreement") on June 26, 2012, and Party B accepted Party A's entrustment to provide consulting, operation and maintenance services relating to online games to Party A.

Now, the Parties have agreed to make the following modifications to the terms concerning dispute settlement and notice in the Original Agreement upon consensus through negotiation:

#### 1. Dispute Settlement

The Parties agree that Clause 13.3 in the Original Agreement shall be changed into: "If a party fails to settle any dispute through negotiation in sixty (60) days upon giving notice to the other party, then either party may submit such dispute to China International Economic and Trade Arbitration Commission for arbitration in Beijing based on then-current arbitration rules. Such award of arbitration is final and binding upon the Parties."

#### 2. Notice

The Parties agree that the contact and fax number of the Parties under Clause 14 in the Original Agreement shall be changed into:

##### **"Party A: Shenzhen 7Road Technology Co., Ltd.**

Contact: Chen Dewen

Fax: 0755-61669777 – 6

##### **Party B: Shenzhen 7Road Network Technologies Co., Ltd.**

Contact: Chen Dewen

Fax: 0755-61669777 – 6"





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In addition to the above modifications, the Parties have reached consensus upon the following terms:

- 1** Matters not contemplated herein shall be governed by relevant provisions in the Original Agreement; in case of conflict arising between the terms in the Original Agreement and those in the Supplementary Agreement, the latter shall prevail.
- 2** The Supplementary Agreement shall come into effect upon the date of signature and seal by the Parties.
- 3** The Supplementary Agreement is executed in four counterparts, and each party shall hold two copies. All counterparts have the same legal force and effect.

**Now, therefore,** the representatives, duly authorized by the Parties, have executed this Agreement as of the date first above written for mutual binding.

(The remainder of this page is intentionally left blank)



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(Intended blank page, serving as signature page of the Supplementary Agreement to Services and Maintenance Agreement)

**Party A: Shenzhen 7Road Technology Co., Ltd.**

Legal representative: /s/ Wang Tao

**Party B: Shenzhen 7Road Network Technologies Co., Ltd.**

Legal representative: /s/ Wang Tao



## Exhibit 4.85



恒生銀行  
HANG SENG BANK

理財創富 專注為你  
Managing wealth for you, with you.

Our Ref: Commercial Banking – A130806

**Confidential**

13 August 2013

Changyou.com Limited  
East Tower Jing Yan Building  
No. 29 Shijingshan Road  
Shijingshan District  
Beijing 100043  
China

Attention: Ms. Jackie Li

Dear Sirs,

**BANKING FACILITIES**

With reference to our recent discussions, we, Hang Seng Bank Limited (the “**Bank**”) have reviewed your banking facilities and are pleased to offer the following revised banking facility/ facilities (the “**Facilities**”) to the borrower(s) specified below (the “**Borrower**”).

The Facilities will be made available on the terms and conditions set out in this letter and the Standard Terms and Conditions for Banking Facilities attached and upon satisfactory completion of the security specified below.

The Facilities are subject to review at any time and in any event by **31 May 2014** and also subject to our overriding right of repayment on demand, including the right to call for cash cover on demand for prospective and contingent liabilities. The Bank shall have an unrestricted discretion to cancel or suspend, or determine whether or not to permit drawings in relation to, the Facilities.

**1. Borrower**

Changyou.com HK Limited  
Changyou.com Limited

**2. Facilities and Limits**

**(I) Facilities available to Changyou.com HK Limited and Changyou.com Limited (“Borrowing Group I”)**

Term Loan Facility (TL)	USD113,000,000
<b>Total</b>	<b>USD113,000,000</b>

恒生銀行有限公司 Hang Seng Bank Limited  
香港中環德輔道中83號 83 Des Voeux Road Central Hong Kong  
網址 Website www.hangseng.com



80 Years of Service Excellence  
用心服務八十年

Member HSBC Group 滙豐集團成員



Changyou.com Limited

Our Ref: Commercial Banking – A130806

(II) Facilities available to Changyou.com Limited (“Borrowing Group II”)

Revolving Loan Facility (RLN)	USD 51,000,000
<b>Total</b>	<b>USD 51,000,000</b>
<b>Grand Total</b>	<b>USD164,000,000</b>

3. Facilities and Conditions

Revolving Loan Facility : Facility Amount: USD51,000,000  
(For Borrowing Group II)

Drawdown: Drawdown can be made in USD, subject to availability as determined at the Bank’s discretion. For any drawdown, Changyou.com Limited shall give the Bank two Business Days prior written notice.

In a minimum amount of USD1,000,000 and an integral multiple of USD500,000.

Availability Period: Subject to the Bank’s periodic review.

Final Maturity Date: 1 year from the date of first drawdown.

Interest Rate and Payment: 1.75% per annum over LIBOR or the Bank’s Cost of Funds, whichever is higher, payable at the end of each interest period or quarterly in arrears if 6 months period is selected. Changyou.com Limited may select an interest period which shall be 1/2/3/6 months. In any event, no interest period shall beyond the Final Maturity Date.

Repayment: Each loan shall be repayable on the maturity date of such loan drawdown unless the Bank allows for a rollover. In any event, no repayment shall beyond the Final Maturity Date.

Prepayment: Voluntary prepayment is not permitted during an interest period.

Condition:

- (i) Changyou.com Limited shall maintain deposits and/or Capital Protection Investment product(s) of not less than the outstanding balance of the RLN facility or its equivalent in other currencies placed in Beijing Branch of Hang Seng Bank (China) Limited (the “Deposits”).



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Changyou.com Limited

Our Ref: Commercial Banking – A130806

(ii) Changyou.com Limited shall ensure that the Deposits and/or Capital Protection Investment product(s) in name of 北京畅游天下网络技术有限公司 (i.e. or Beijing AmazGame Age Internet Technology Co. Ltd.).

(iii) The Deposits and/or Capital Protection Investment product(s) can be released subject to this facility fully repaid.

Term Loan Facility  
(For Borrowing Group I)

: Loan Account No.: 337-040802-302

Outstanding Loan Amount: USD113,000,000 as of 12 August 2013

Original Loan Amount: USD150,000,000

Final Maturity Date: 17 September 2014

Interest Rate and Payment: 2.4% per annum over LIBOR or the Bank's Cost of Funds, whichever is higher, payable at the end of each interest period or quarterly in arrears if 6/12 months period is selected. The Borrower may select an interest period which shall be 1/3/6/12 month(s). No Interest Period shall extend beyond the Final Maturity Date.

With effect from 17 September 2013, the interest rate will be changed to 1.75% per annum over LIBOR or the Bank's Cost of Funds, whichever is higher, payable at the end of each interest period or quarterly in arrears if 6/12 months period is selected. The Borrower may select an interest period which shall be 1/3/6/12 month(s). No Interest Period shall extend beyond the Final Maturity Date.

Repayment: Principal to be repaid in one lump sum on the Final Maturity Date.

All sums which may become due to the Bank from time to time in respect of this facility (including but not limited to principal and interest) are to be directly debited from the account maintained with the Bank.

Prepayment: Prepayment (in whole or in part) is allowed provided that the Bank receives 7 Business Days' prior written notice and such prepayment is made on an interest payment date.

3

恒生銀行有限公司 Hang Seng Bank Limited

Member HSBC Group 滙豐集團成員



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Changyou.com Limited

Our Ref: Commercial Banking – A130806

Condition(s):

- (1) The Borrower shall maintain deposits not less than the outstanding balance of the TL facility or its equivalent in other currencies placed in Beijing Branch of Hang Seng Bank (China) Limited (the "Deposits I").
- (2) The Borrower shall ensure that the Deposits I in name of 北京畅游天下网络技术有限公司 (i.e. or Beijing AmazGame Age Internet Technology Co. Ltd.).
- (3) The Deposits I can be released subject to this facility fully repaid.

**4. Security****The Bank shall continue to hold:-**

For the Borrower

- (1) **Cross Guarantee** dated 5 August 2012 for USD150,000,000 from the Borrower for TL facility only.

**5. Undertakings****The Borrower and the under-mentioned undertaking parties (if any) shall continue to undertake to the Bank as follows:-**

- (1) Changyou.com Limited shall remain its listing status in NASDAQ and its shares shall not be suspended for trading for more than 10 consecutive trading days, unless getting the Bank's consent.
- (2) Changyou.com HK Limited shall remain 100% directly or indirectly owned by Changyou.com Limited.
- (3) The Borrower shall ensure that the depositor 北京畅游天下网络技术有限公司 (i.e. or Beijing AmazGame Age Internet Technology Co. Ltd.) shall be directly or indirectly owned by Changyou.com HK Limited.
- (4) The Borrower undertakes that for any Facilities denominated in Renminbi (if any), it will not directly or indirectly on-lend the proceeds of such Facilities to (i) any individuals and (ii) any Designated Business Customers if the proceeds of such Facilities (or any other Renminbi proceeds derived therefrom) are directly or indirectly credited to Renminbi accounts for the category of Designated Business Customers which are maintained for limited purposes of handling Renminbi cashnotes obtained in their ordinary course of business as Designated Business Customers and for Renminbi bond investment.

4

恒生銀行有限公司 Hang Seng Bank Limited

Member HSBC Group 滙豐集團成員





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**Changyou.com Limited****Our Ref: Commercial Banking – A130806**

“Designated Business Customers” means establishments that have had a business relationship with a Hong Kong Renminbi business participating bank for more than three years which engage in commercial retail, catering, accommodation, transportation services, communications services, medical services, or educational services, including such establishments that have had a business relationship with such participating bank for less than three years, but with concrete evidence to show that they have the actual relevant business background.

The Borrower shall and agree to indemnify the Bank for all losses and liabilities incurred or suffered by the Bank arising out of or in connection with any breach of the above undertaking by the Borrower.

- (5) The Borrower and the corporate guarantor(s) (if any) shall provide to the Bank a certified copy of its annual audited accounts/financial statements within 180 days after the end of each financial year and such other relevant financial information as the Bank may from time to time reasonably request.
- (6) Each of the Borrower and the corporate guarantor(s) (if any) and the corporate security provider(s) (if any) shall immediately inform the Bank once there are changes of its directors or beneficial shareholders or amendment to its memorandum and articles of association or equivalent constitutional documents and shall ensure that such changes/amendment are updated in the company registry of its place of incorporation promptly.

**6. Fees**

Upon completing each review of the Facilities, the Bank is authorised to debit the current account maintained by the Borrower with the Bank for the facility review fee as the Bank may prescribe from time to time.

If applicable, a valuation fee shall be payable by the Borrower for the purpose of valuation of the property by surveyor appointed by the Bank in its sole discretion. The Bank is authorised to debit the current account maintained by the Borrower with the Bank for such valuation fee as the surveyor may charge, notwithstanding that the Borrower does not accept this Facility Letter, the Facilities are not made available due to the Borrower failing to comply with the terms and conditions set out in this Facility Letter, or the Facilities are cancelled or suspended at any time.

**Section 83 of the Banking Ordinance**

Section 83 of the Banking Ordinance (Cap. 155, Laws of Hong Kong) has imposed on us as a bank certain limitations on advances to persons related to our directors or employees. In accepting the Facilities, the Borrower should advise us whether the Borrower is in any way related to any of our directors or employees within the meaning of Section 83 and in the absence of such advice we will assume that the Borrower is not so related. We would also ask that if the Borrower becomes so related subsequent to accepting the Facilities, the Borrower should immediately advise us in writing.

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恒生銀行有限公司 Hang Seng Bank Limited

Member HSBC Group 滙豐集團成員



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**Changyou.com Limited****Our Ref: Commercial Banking – A130806**

Please note that in reviewing the application, we may make reference to the credit report(s) of the Borrower(s)/guarantor(s)/security provider(s) (as the case may be) from the credit reference agency(ies). If you wish to access the report(s) yourself, you can contact the credit reference agency(ies) directly at the following address:

Commercial credit reference agency:

Dun & Bradstreet (HK) Ltd., Unit 1308-1315, 13/F., BEA Tower, Millennium City 5, 418 Kwun Tong Road, Kwun Tong, Kowloon.

Tel: 2516 1100; Fax: 2960 4721.

Please arrange for the enclosed copy of this letter to be signed by the Borrower and all guarantors and security providers of the Facilities and return the same to the Bank with Board Resolution(s) and Shareholder's Resolution(s) (if applicable) of the Borrower and all guarantors and security providers before **13 September 2013**, failing which our offer shall lapse unless it is extended by us at our absolute discretion.

By accepting this Facility Letter, you would agree to channel all your remittance transactions and insurance arrangement to the Bank. Our Cash Management & Payment Services Department and Commercial Sales Department would contact you to offer our services on remittance and insurance respectively.

Should you have any queries, please do not hesitate to contact the following persons:-

Queries on	Name	Telephone No.
Banking arrangement	Ms. Chui Sze Ka Bianca	21985223
Factoring arrangement	Ms. Joan Kwan	21988678
Insurance	Mr. Stanley Ng	36625056
	Mr. John Li	21982522
Remittance	Mr. Billy Chow	21984534
	Remittance Hotline	21986919
Wealth management	Ms. Joey Tsang	21985534
Execution of documents	Documentation Hotline	21982094

Kindly return the accepted Facility Letter and executed documents to **Credit Operations Manager, Credit Operations Department, L21, Tower 2, Enterprise Square V, 38 Wang Chiu Road, Kowloon Bay, Kowloon, Hong Kong.**

We trust that you will make active use of the Facilities and are pleased to be of continued assistance.

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**Changyou.com Limited****Our Ref: Commercial Banking – A130806**

Yours faithfully,  
For Hang Seng Bank Limited

\_\_\_\_\_  
Jessica Hung  
Senior Vice President  
Portfolio Management and Compliance  
Corporate and Commercial Banking

\_\_\_\_\_  
Jones Chung  
Vice President  
Portfolio Management and Compliance  
Corporate and Commercial Banking

HM/mh

I/We hereby accept the Facilities and agree to be bound by all the terms and conditions set out in this letter and the Standard Terms and Conditions for Banking Facilities, which I/we have read and understood.

\_\_\_\_\_  
Changyou.com HK Limited

\_\_\_\_\_  
Changyou.com Limited

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恒生銀行有限公司 Hang Seng Bank Limited

Member HSBC Group 滙豐集團成員



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**Exhibit 4.86**

Our reference number: FL993A\_Changyou.com\_new

26<sup>th</sup> July, 2013

Confidential

Changyou.com Limited  
East Tower, Jing Yan Building  
No. 29 Shijingshan Road  
Shijingshan District  
Beijing 100043, PRC

Attn: Mr. Alex Ho

Dear Sirs,

Re: Changyou.com Limited  
US\$100 Million Term Loan Facility

This letter (this "Facility Letter") sets out the terms and conditions upon which The Bank of East Asia, Limited will provide a US\$100,000,000.00 term loan facility to Changyou.com Limited.

**(1) Borrower:**

Changyou.com Limited, a company incorporated in Cayman Islands and having its registered office at Offshore Incorporations (Cayman) Limited, Scotia Centre, 4<sup>th</sup> Floor, P.O. Box 2804, George Town, Grand Cayman KY1-1112, Cayman Islands (the "Borrower").

**(2) Lender:**

The Bank of East Asia, Limited, whose registered office is situated at No. 10 Des Voeux Road Central, Hong Kong (the "Lender").

**(3) Nature and Facility Amount:**

A term loan facility (the "Facility") of up to a maximum principal amount of US\$100,000,000.00 (United States Dollars One Hundred Million Only) (the "Facility Limit").

**(4) Purpose:**

To finance dividend distribution, overseas investment and working capital for offshore operation.

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**(5) Final Maturity Date:**

Subject to the Lender's customary overriding right of repayment on demand as stipulated in Paragraph (13) below, the final maturity date of each drawing/advance under the Facility (the "Final Maturity Date of each Advance") shall be (i) the date falling 14 days before the expiry date of the respective Standby L/C (as hereinafter defined in Paragraph (14) below) supporting such drawing/advance or (ii) the date falling 12 months from the date of first drawing under the Facility (the "First Drawdown Date"), whichever is earlier.

**(6) Drawing/Availability:**

The Facility is available for multiple drawings on any Business Day within 6 months (the "Availability Period") from the date of the Lender's receipt of the Borrower's acceptance of this Facility Letter provided that:-

- (i) The Lender shall have received in form and substance satisfactory to it all of the documents and other evidence as listed in the "Conditions Precedent" as stipulated in Paragraph (7) hereof;
- (ii) Each drawing shall be in a minimum amount of US\$5,000,000.00 and if for a larger amount, an integral multiple of US\$2,000,000.00;
- (iii) The Borrower shall have given not less than 3 Business Days' prior written notice of drawing to the Lender specifying the date and the amount of the proposed drawing;
- (iv) Each drawing shall have been supported by the respective Standby L/C issued by the Issuing Bank (as hereinafter defined in Paragraph (14) below) in RMB for an amount not less than 100% of the corresponding amount of drawing with reference to the prevailing exchange rate determined at the sole discretion of the Lender;
- (v) The total loan(s) outstanding after taking into account of the amount of the proposed drawing(s) shall not exceed the Facility Limit;
- (vi) The maximum number of drawings shall not exceed 8; and
- (vii) Any undrawn balance at the end of the Availability Period will be cancelled automatically.

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The Lender reserves the sole and absolute right to (i) prescribe any conditions subject to which it provides any services and/or the Facility; (ii) refuse to take any instruction, to provide any services and/or the Facility or to act on any instruction; and (iii) take any actions (including but not limited to the recourse to the Borrower or suspension, termination or closure of the Facility/relevant account(s)) to ensure its compliance with any anti-money laundering, counter-terrorist financing or other similar requirements, other applicable laws, rules, regulations, guidelines, requests and/or recommendations. The Lender will not be liable for any loss caused in whole or in part by any actions/matters which may delay or prevent the processing of any instructions relating to this Facility Letter and the Facility due to the Lender's fulfillment of any anti-money laundering, counter-terrorist financing or other similar requirements under applicable laws and regulations.

**(7) Conditions Precedent:**

The obligation of the Lender to make available the Facility to the Borrower hereunder is conditional upon:

- (a) The Borrower having furnished to the Lender, prior to the First Drawdown Date, the following in form and substance satisfactory to the Lender:
- (i) Certified true copy of the Borrower's Certificate of Incorporation, Certificate of Incorporation on Change of Name (if any), Certificate of Incumbency, Certificate of Good Standing and updated Memorandum and Articles of Association (or applicable constitutional documents);
  - (ii) Certified true copy of the resolutions (with copy list of specimen signature(s) of authorised signatory(ies) enclosed thereon) duly passed at a duly convened and held meeting of the Board of Directors of the Borrower evidencing (i) the approval of the Facility, (ii) the acceptance of the terms and conditions of this Facility Letter to which the Borrower is a party and (iii) the authorization of appropriate officer(s) to countersign this Facility Letter and to sign on behalf of the Borrower all confirmations, notice of drawing and other notices, requests or other communications required to be made and given to the Lender hereunder or otherwise in connection with the Facility;

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Changyou.com Limited

- (iii) The duplicate of this Facility Letter duly signed by the authorised signatory(ies) of the Borrower;
  - (iv) Copy of Hong Kong Identity Card or passport of each of the officers of the Borrower authorised to sign the documents as referred to in sub-paragraphs (ii) and (iii) hereinabove;
  - (v) Process Agent Appointment Letter duly signed by the Process Agent (as hereinafter defined in Paragraph (27) below); and
  - (vi) Such other documents and conditions as the Lender may request or prescribe.
- (b) The Lender being satisfied with the corporate power and legal capacity of the Borrower to enter into the documents as referred to in sub-paragraphs (a)(iii) hereinabove and for this purpose, the Lender may require legal opinions or such other documents relating to any of the matters contemplated herein to be provided in form and substance satisfactory to the Lender at the expense of the Borrower.
- (c) There being no material adverse change in the financial market condition and in the financial condition of the Borrower.

**(8) Interest Rate:**

- (a) Normal Interest
- (i) Interest on all the loan(s) outstanding of the Facility shall be calculated at the rate of 1.50% (the "Margin") per annum over London Interbank Offered Rate ("LIBOR") as quoted by the Lender 2 Business Days before the date of each drawing or the date of rollover for an interest period of 1, 2 or 3 months (the "Interest Period") as selected by the Borrower. Interest shall be calculated on the basis of the actual number of days elapsed on a 360-day year. Interest accrued shall be payable in arrear by the Borrower on the last Business Day of each Interest Period (each an "Interest Payment Date") and on the Final Maturity Date of each Advance provided that no Interest Period shall extend beyond the Final Maturity Date of each Advance. In the absence of nomination of Interest Period by the Borrower, the Interest Period of the proposed drawdown/rollover shall be of 1-month duration; and

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- (ii) There shall not be more than 3 Interest Periods outstanding at any one time, and if there have already been 3 Interest Periods outstanding at any one time, any Interest Period commencing thereafter shall end on the last day of any of the then current Interest Periods to be selected by the Borrower and specified in its relevant notice of drawing or (for subsequent roll-over) notice in writing received by the Lender at least 3 Business Days prior to commencement of the relevant Interest Period, and in the absence of such selection, it shall end on the last day of the then current Interest Period which is the last to expire.

(b) Default Interest

In respect of the loan(s) outstanding under the Facility, interest thereon and other sums in respect of the Facility not repaid or paid on the due date or dates provided hereunder, interest shall be payable on demand from the due date or dates for payment thereof until the date of actual payment in full of such loan(s) outstanding and/or interest and/or other sums (as the case may be) at the rate of 5% per annum over the rate of interest as determined by the Lender in accordance with sub-paragraph (a) of this Paragraph (8) (both before and after judgement). For so long as the default continues, the relevant rate of interest shall be re-determined by the Lender on the same basis thereafter and shall be compounded at weekly intervals.

(9) **Arrangement Fee:**

Waived.

(10) **Undrawn Balance Fee:**

Waived.

(11) **Repayment:**

Subject to Paragraph (13) hereinbelow, all outstanding amounts of each drawing/advance of the Facility including but not limited to the principal outstanding, the accrued interest and any other sums owing to the Lender shall be repaid in full on the Final Maturity Date of each Advance. Amount repaid is not available for re-drawing.

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**(12) Voluntary Prepayment:**

The Borrower may on any Interest Payment Date commencing from the 7<sup>th</sup> month after the First Drawdown Date prepay in whole or in part the loan(s) outstanding under the Facility provided that:

- (a) Prepayment is not allowed for the first 6 months after the First Drawdown Date;
- (b) The Borrower shall have given not less than 5 Business Days' prior written notice of prepayment to the Lender, specifying the amount to be prepaid and the date of such prepayment;
- (c) Each partial prepayment shall be in a minimum amount of US\$5,000,000.00 and if for a larger amount, an integral multiple of US\$2,000,000.00;
- (d) Each prepayment shall be made together with accrued interest on the amount prepaid and any other amounts (including but not limited to funding loss, if any) payable by the Borrower in respect thereof on the date of prepayment. The breakage funding cost shall be payable by the Borrower if prepayment is not made on an Interest Payment Date; and
- (e) Amount prepaid is not available for re-drawing.

**(13) Lender's Overriding Rights:**

Notwithstanding anything contained herein to the contrary (in particular, Paragraphs (5) and (11)), the Facility is subject to the Lender's review, amendment of any terms and/or cancellation of all or any part thereof from time to time at the sole discretion of the Lender and the loan(s) outstanding, interest thereon and any other sums owing or payable under the Facility are subject to the Lender's customary overriding right of repayment on demand. The Lender hereby expressly reserves the unfettered right of terminating the Facility and/or requiring repayment of all monies owing from or payable by the Borrower to the Lender at any time by notice in writing to the Borrower, whereupon the Facility or any part thereof as stipulated in the Lender's notice shall forthwith be terminated and/or all monies owing from or payable by the Borrower to the Lender or any part thereof as stipulated in the Lender's notice shall forthwith be repaid by the Borrower.

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**(14) Security:**

Standby Letter of Credit(s) (the “Standby L/C”) in form and substance as approved by the Lender for the amount of not less than 100% of the amount of corresponding advance(s) under the Facility in RMB with reference to the prevailing exchange rate determined at the sole discretion of the Lender, to be issued by The Bank of East Asia (China) Limited, Beijing Branch (the “Issuing Bank”) in favour of the Lender as the beneficiary, whereby the Issuing Bank shall honour its payment obligation to the Lender up to the amount as stipulated in the Standby L/C upon and subject to the terms and conditions contained therein.

(This Facility Letter and the Standby L/C are collectively referred to as the “Finance Documents”).

**(15) Payments:**

- (a) On the date of each drawing under the Facility, the Lender shall make the advance available to the Borrower by crediting the same in United States Dollars in same day funds to the account designated in the irrevocable notice of drawing given by the Borrower or in such other manner as the Borrower may specify in the irrevocable notice of drawing given by the Borrower (provided that such other manner as specified by the Borrower must be acceptable to the Lender);
- (b) On each date on which any sum is due or payable by the Borrower under or in connection with the Facility, the Borrower shall either (i) make such sum available before 11:00 a.m. (Hong Kong time) in same day funds in its CorporatePlus account maintained with the Lender (Account No.: 015-514-68-00423-4) (the “CorporatePlus Account”), (ii) by CHATS before 11:00 a.m. (Hong Kong time) in same day funds to the Lender’s account no. 015-514 (S.W.I.F.T. BEASHKHH) or (iii) in such other manner as instructed by the Lender. The Borrower hereby irrevocably authorises the Lender to debit the Current Account on any date on which any sum is due or payable under or in connection with the Facility without further consent from or notice to the Borrower;
- (c) Whenever any payment under this Facility Letter (including but not limited to the principal repayment and interest payment) or otherwise in connection with the Facility shall become due on a day which is not a Business Day, the due date thereof shall be extended to the next Business Day in the same calendar month (if there is one) or on the preceding Business Day (if there is no succeeding Business Day in the same calendar month);

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- (d) All payments by the Borrower hereunder shall be made free and clear of any deduction or withholding on account of tax, levy, impost, duty or charges of whatsoever nature ("Tax Payment"). The Borrower shall as soon as practicable deliver to the Lender relevant receipts for any Tax Payment required to be made by it. If any withholding or deduction is required, the amount to be paid by the Borrower must be increased to the extent that the Lender will receive such amount as it would otherwise have been entitled to receive had there been no such deduction or withholding;
- (e) If for any reason (including but not limited to insolvency, breach of fiduciary or statutory duties, fulfillment of any anti-money laundering, counter-terrorist financing or other similar requirements under any applicable law and regulations, or any other similar event) (i) any payment to the Lender (whether in respect of the obligations and/or indebtedness of the Borrower or any security for those obligations and/or indebtedness or otherwise) is avoided, reduced or required to be restored, or (ii) any discharge, compromise or arrangement (whether in respect of the obligations and/or indebtedness of the Borrower or any security for those obligations and/or indebtedness or otherwise) is given or made wholly or partly on the basis of any payment, security or other matter which is avoided, reduced or required to be restored, then (a) the liability of the Borrower shall continue (or be deemed to continue) as if the payment, discharge, compromise or arrangement had not occurred, and (b) the Lender shall be entitled to recover the value or amount of that payment or security from the Borrower, as if the payment, discharge, compromise or arrangement had not occurred; and
- (f) Any release, discharge or settlement between the Borrower and the Lender shall be conditional upon no security, disposition or payment to the Lender by the Borrower being void, set aside, ordered to be refunded, retained or held on suspense pursuant to any enactment or applicable law relating to bankruptcy, liquidation, administration or insolvency or any enactment or applicable law relating to anti-money laundering or anti-terrorism financing or other similar requirements or for any other reason whatsoever and if the aforesaid condition shall not be fulfilled, the Lender shall be entitled to enforce the Finance Documents subsequently as if such release, discharge or settlement had not occurred and any such payment had not been made.

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**(16) Market Disruption:**

Notwithstanding anything contained herein to the contrary (in particular, Paragraph (8)), if the Lender, on the date of each drawing under the Facility or on each subsequent Interest Payment Date, notifies the Borrower that its cost of obtaining matching deposits in the relevant interbank market in relation to a drawing/rollover under the Facility would be in excess of LIBOR for the relevant Interest Period, then the rate of interest on such drawing/rollover payable by the Borrower for the relevant Interest Period ("Alternative Interest Rate") shall be (i) the annual percentage rate quoted by the Lender as its cost in funding that drawing/rollover (which shall be conclusive and binding on the Borrower, save for any manifest error) plus (ii) the Margin as referred to in Paragraph (8)(a)(i).

The Borrower shall be at liberty after receipt of such notice from the Lender to prepay to the Lender in whole (but not in part) the loan (s) outstanding, interest thereon and any other sums owing or payable under the Facility (subject to sub-paragraphs (12)(d) to (e) and (25)(a)) provided that the Borrower shall have given to the Lender not less than 15 Business Days' prior written notice of its intention of making full prepayment of the outstanding loan(s), interest thereon and other indebtedness under the Facility.

**(17) Increased Costs:**

If as a result of (i) the introduction of or any change in (or in the interpretation, administration or application of) any law or regulation (which shall include, without limitation, any law or regulation concerning capital adequacy, prudential limits, liquidity, reserve assets or tax); or (ii) compliance with any law, regulation, direction, request or requirement (whether or not having the force of law) of any competent governmental or other authority made after the date of this Facility Letter, any increased costs are incurred or suffered by the Lender, which shall include (1) a reduction in the rate of return from the Facility or on the Lender's overall capital (including, without limitation, as a result of any reduction in the rate of return on capital brought about by more capital being required to be allocated by the Lender); and/or (2) a reduction of any amount due and payable under the Finance Documents ("Increased Costs"), the Borrower shall:

- (a) pay on demand to the Lender such additional amounts as the Lender may certify (which certificate shall be conclusive and binding on the Borrower, save for any manifest error) to be necessary to compensate the Lender for such Increased Costs; and

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- (b) be at liberty at any time after its receipt of any such demand and so long as the circumstances giving rise to such Increased Costs may continue and subject to its giving to the Lender not less than 15 Business Days' prior written notice, to prepay to the Lender in whole (but not in part) the loan(s) outstanding, interest thereon and any other sums owing or payable under the Facility (subject to sub-paragraphs (12)(d) to (e) and (25)(a)).

Any demand as referred to in sub-paragraph (a) of this Paragraph (17) may be made at any time before or after the end of any period or any time before or after any prepayment or repayment of all or part of the Facility to which such demand relates.

#### (18) Representations and Warranties:

The Borrower represents and warrants to the Lender throughout the whole term of the Facility and for so long as any amount is outstanding under the Facility that:

- (a) The Borrower has the corporate power and authority to (i) borrow the Facility from the Lender on the terms and conditions herein and (ii) give security /indemnity/assurance as support for the borrowing of the Facility from the Lender, and no event, state of affairs, conditions or act which constitutes or with the passing of time, giving of notice, or with the fulfillment of any condition will or may constitute an Event of Default (as defined in Paragraph (20) below) has occurred or will occur on the date of making a drawing by the Borrower under the Facility or as a result thereof;
- (b) The Borrower (i) is duly incorporated and validly existing under the laws of its place of incorporation and (ii) has full legal right, capacity, power and authority to enter into the Finance Documents to which it is party and (iii) has taken all necessary actions to authorise the borrowing of the Facility on the terms and conditions hereunder;
- (c) This Facility Letter, when signed/executed by the Borrower, will constitute legal, valid and binding obligations of the Borrower enforceable against the Borrower in accordance with the terms herein;
- (d) The Borrower's entering into this Facility Letter does not and will not violate or exceed any borrowing or similar limit or other power or restriction granted or imposed by any law to which the Borrower is subject or under its Memorandum and Articles of Association (or applicable constitutional documents);

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- (e) The Borrower's entering into, exercising of its rights and/or performing of or complying with its obligations under this Facility Letter does not and will not violate, to an extent or in a manner which has or is likely to have a material adverse effect on its financial condition or operation, any agreement to which it is a party or which is binding on it or its assets;
- (f) Any information (written or otherwise) provided by the Borrower in connection with the Facility and the financial condition of the Borrower is/are true and accurate as of the date of providing them;
- (g) The Borrower's obligations under this Facility Letter are direct, unconditional and unsubordinated obligations of the Borrower and rank at least pari passu with all other present and future unsecured borrowings of the Borrower, save as otherwise provided by law;
- (h) The representations and warranties contained in sub-paragraphs (a) to (g) of this Paragraph (18) shall be deemed to be repeated and will remain to be true and accurate in all respects as if made on each date on which any amount is outstanding under the Facility or any part of the Facility remains available or subsisting.

**(19) Undertakings:**

The Borrower undertakes to the Lender throughout the whole term of the Facility and for so long as any sum remains owing or payable under the Facility that:

- (a) The Borrower shall deliver to the Lender its (i) audited consolidated financial statements as soon as available and in any event within 120 days after the end of each of its financial years, and (ii) interim half-year unaudited consolidated financial statements as soon as practicable and in any event within 90 days after the end of the relevant first 6-month period in its financial years;
- (b) The Borrower shall deliver to the Lender any circular, document or other information (written or otherwise) as the Lender may from time to time reasonably request;
- (c) The Borrower shall maintain its corporate existence and conduct its business and operations in compliance with all applicable laws and in a proper manner;

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- (d) The Borrower shall maintain (i) 100% beneficial ownership of the issued share capital of Changyou.com HK Limited, a company incorporated in Hong Kong and having its registered office at 12<sup>th</sup> Floor, Ruttonjee House, No. 11 Duddell Street, Central, Hong Kong ("Changyou.com HK") and Beijing AmazGame Age Internet Technology Co., Ltd, a company incorporated in the People's Republic of China and having its registered office at Room 1210, Building 3, No. 3 Badachu High-tech Science Park, Shijingshan District, Beijing, the People's Republic of China ("Beijing AmazGame") and (ii) the management control of Changyou.com HK and Beijing AmazGame;
- (e) The shares of the Borrower shall remain listed on the NASDAQ Global Select Market and shall not be suspended from trading on NASDAQ Global Select Market for a period exceeding consecutive 14 trading days except for obtaining approval in writing from the Lender;
- (f) The Borrower represents, declares and undertakes to the Lender that the utilization of any Facility or use of Facility proceeds drawn under this Facility Letter do not and will not conflict with any law or regulation applicable to the Borrower (including without limitation those in force in the People's Republic of China). The above representation and declaration are deemed to be made by the Borrower by reference to the facts then existing during the period where the Facility or any part thereof remain outstanding;
- (g) The Borrower shall forthwith notify the Lender in writing of (i) the occurrence of any Event of Default as referred to in Paragraph (20) below and/or (ii) the occurrence of any event, state of affairs, conditions or act which with the passing of time, giving of notice, or with the fulfillment of any condition will or may constitute an Event of Default; and
- (h) The Borrower shall promptly upon the request of the Lender supply, or procure the supply of, such documentation and other evidence as is reasonably requested by the Lender in order for the Lender to conduct any "Know Your Customer" or other similar procedures under applicable laws and regulations.

**(20) Events of Default:**

Upon the occurrence of any of the following events at any time (each an "Event of Default"):

- (a) The Borrower fails to pay on the due date to the Lender any sum (including but not limited to any repayment of principal and interest payment) that the Borrower is obliged to pay in connection with the Facility; or

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- (b) The Borrower defaults in the performance of any other obligations hereunder and/or under the Finance Documents (as the case may be); or
- (c) The Borrower becomes insolvent or any liquidator/trustee in bankruptcy or receiver has been appointed over all or part of the assets of the Borrower or the Borrower is unable or admits inability to pay its debts as they fall due; or
- (d) There occurs, in the opinion of the Lender, a material adverse change in the financial condition of the Borrower or there occurs, in the opinion of the Lender, any situation which has materially and adversely affected or may materially and adversely affect the ability of the Borrower to perform any or all of its obligations hereunder; or
- (e) A petition is presented or a proceeding is commenced or an order is made or an effective resolution is passed or any other step is taken by any person for the winding-up, insolvency, administration, reorganization, reconstruction, dissolution or bankruptcy of the Borrower or for the appointment of a liquidator, receiver, administrator, trustee or similar officer of the Borrower or of all or any part of its business or assets; or
- (f) Any indebtedness of the Borrower becomes due before its stated maturity or when called, or the Borrower defaults under or commits a breach of any instrument or agreement relating to any such indebtedness; or
- (g) Any step is taken by any person for the purpose of a reconstruction, amalgamation, reorganization, merger or take-over involving the Borrower (except for a solvent merger or take-over on terms approved by the Lender in writing before such step is taken); or
- (h) The Borrower ceases to maintain (i) 100% beneficial ownership of the issued share capital of Changyou.com HK and Beijing AmazGame and/or (ii) the management control of Changyou.com HK and Beijing AmazGame; or
- (i) The shares of the Borrower, for any reason (other than technical in nature as determined by the Lender in its sole discretion) cease or are suspended from trading on NASDAQ Global Select Market for more than 14 consecutive trading days except for obtaining approval in writing from the Lender; or

.../14



Page 14  
 Changyou.com Limited

- (j) Any representation, warranty, undertaking or statement made by the Borrower hereunder is not complied with or is or proved to be incorrect or misleading in any material respect when made, repeated or deemed to be repeated; or
- (k) There occurs any event or circumstance which, with the giving of notice and/or the lapse of time and/or the making of any necessary determination under this Facility Letter and/or the satisfaction of any applicable condition, or any combination of any of the foregoing might constitute an Event of Default;

then the Lender may, at any time when any one of the above-mentioned Events of Default occurs and/or is continuing, terminate the Facility and demand immediate payment and/or repayment of all amounts outstanding (together with interest accrued thereon and any other amounts owing to the Lender) under or in connection with the Facility from the Borrower.

This Paragraph (20) is without prejudice to the Lender’s overriding rights as set out in Paragraph (13) above.

**(21) Set-off:**

- (a) The Borrower hereby irrevocably authorises the Lender to apply (without prior notice) any credit balance (whether or not then due) to which the Borrower is at any time beneficially entitled on any account at, any sum held to the order of the Borrower by and/or any liability of any office of the Lender, either singly or jointly, in or towards satisfaction of any sum then due from the Borrower to the Lender in connection with the Facility and unpaid. For this purpose, the Lender is authorised to use all or any part of any such credit balance to buy such other currencies as may be necessary to effect such application.
- (b) The Lender shall not be obliged to exercise any of its rights under this Paragraph (21), which shall be without prejudice and in addition to any right of set-off, combination of accounts, lien or other right to which it is at any time otherwise entitled (whether by operation of law, contract or otherwise).



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Changyou.com Limited

**(22) Severability:**

Any provision of this Facility Letter prohibited by or becoming unlawful or unenforceable under any applicable law actually applied by any court of competent jurisdiction shall, to the extent required by such law, be severed from this Facility Letter and be rendered ineffective so far as is possible without modifying the remaining provisions of this Facility Letter. Where, however the provisions of any such applicable law may be waived, they are hereby waived by the parties hereto to the full extent permitted by such law to the effect that this Facility Letter shall be a valid and binding agreement enforceable in accordance with its terms.

**(23) Entire Agreement:**

This Facility Letter constitutes the entire agreement of the Lender and the Borrower and supersedes any previous expressions of intent or understanding in respect of the Facility.

**(24) Expenses:**

All costs, charges, taxes, fees and expenses (including legal fee on a full indemnity basis) incurred by the Lender in connection with the preparation, negotiation, administration, execution, perfection, enforcement and/or amendment of, supplement to or waiver in respect of the Finance Documents and all other relevant documents or otherwise in connection with the Facility shall be borne and paid by the Borrower on demand, irrespective of whether or not any part of the Facility is subsequently utilized.

**(25) Indemnity:**

- (a) The Borrower shall on demand indemnify the Lender in full against any cost, loss, expense, tax, fee, claims, proceeding or liability whatsoever incurred, suffered or sustained and as conclusively certified by the Lender as a result of (i) any drawing not being made following the giving of a notice of drawing by the Borrower due to non-fulfillment of any condition of this Facility Letter, or (ii) the making of any drawing pursuant to this Facility Letter or otherwise, or (iii) any prepayment under the Facility on a non-interest Payment Date.
- (b) The Borrower shall fully indemnify the Lender for any cost, loss or liability incurred by the Lender as a result of any actions taken by the Lender in connection with the fulfillment of anti-money laundering, counter-terrorist financing or other similar requirements under applicable laws and regulations.
- (c) If any amount is received or recovered in a currency other than the currency (the "Account Currency") in which payment has been demanded pursuant to the Finance Documents (whether as a result of, or of the enforcement of, a judgment or order of a court, tribunal or authority of any jurisdiction, or in the dissolution of the Borrower or otherwise), it shall only constitute a discharge by the Borrower to the extent of the amount in the Account Currency which the Lender is able to purchase with the amount so received or recovered in that other currency on the date of receipt or recovery. If that amount is less than the Account Currency amount expressed to be due to the Lender, the Borrower shall on demand indemnify the Lender against any loss/shortfall sustained by it as a result.

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Changyou.com Limited

**(26) Evidence:**

Any certificate issued by the Lender as to the amount of the loan(s) outstanding, the rate of interest applicable to the amount of any sums owing or payable in connection with the Facility or any other matters relating to this Facility Letter shall, save to the extent of manifest error, be conclusive evidence against the Borrower as to the matter(s) covered thereby.

**(27) Process Agent:**

The Borrower irrevocably appoints Changyou.com HK to be its agent (the “Process Agent”) for the service of process in Hong Kong. Any documentation in connection with the proceedings in the courts of Hong Kong delivered to the Process Agent at its registered office from time to time shall be treated as duly delivered to and served on the Borrower. The Borrower shall procure the Process Agent to forthwith notify the Lender in writing of any change in the address of its registered office.

**(28) Governing Law and Jurisdiction:**

This Facility Letter and all other relevant documents and the rights and obligations of the Lender and the Borrower hereunder/thereunder shall be governed by and construed in accordance with the laws of the Hong Kong Special Administrative Region of the People’s Republic of China (“Hong Kong”) and each party hereto hereby irrevocably submits to the non-exclusive jurisdiction of the courts of Hong Kong.

**(29) Miscellaneous:**

(a) Reference to the time of a day is to Hong Kong time (unless otherwise stated), and time is of the essence hereof;



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Changyou.com Limited

- (b) "Business Day" as used in this Facility Letter means a day (other than Saturday and Sunday) on which dealings in United States Dollars may be carried out in the relevant interbank market and on which banks are generally open for business in Hong Kong, London and New York;
- (c) For the purpose of this Facility Letter, any determination as to whether any event, situation, circumstance or document is "material", "adverse", "reasonable", "expedient" or "necessary" shall be determined by the Lender whose determination shall be conclusive and binding on the Borrower;
- (d) Without prejudice to the Lender's overriding rights in any other provisions of this Facility Letter, the Lender may revise or vary the terms applicable to the Facility if there is any (i) material adverse change or deterioration in respect of the financial condition or position of the Borrower at any time as determined by the Lender at its sole and absolute discretion or (ii) downgrade of the credit rating of the Borrower as announced by any credit rating agency from time to time; and
- (e) Headings on this Facility Letter are for ease of reference only and shall not affect the interpretation of the terms and conditions of this Facility Letter.

Please signify your acceptance of the above terms and conditions by signing and returning to us the duplicate of this Facility Letter within 2 weeks from the date hereof, failing which our offer will automatically lapse. Upon our receipt of your acceptance of this Facility Letter, this Facility Letter will be legally binding upon your goodselves as the Borrower and this Bank as the Lender with immediate effect.

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Changyou.com Limited

If you have any query in relation to the terms and conditions of this Facility Letter, please feel free to contact our Christine Wong or Liu Kai Cheong of Corporate Lending and Syndication Department at 3608 0968 or 3608 0991.

Yours faithfully,

For and on behalf of

The Bank of East Asia, Limited

Jennifer Leung

Officer

Trade and Loan Services Department

Operations Support and Services Division

Sally Lam

Senior Credit Administration Manager

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Page 19  
Changyou.com Limited

In consideration of the Lender agreeing to grant to the Borrower the Facility pursuant to the terms and conditions of this Facility Letter:-

The Borrower

We hereby agree to be bound by and accept all the terms and conditions of this Facility Letter.

For and on behalf of  
Changyou.com Limited

\_\_\_\_\_  
Name:  
Date:

Witness:

The Process Agent

We hereby agree to the appointment as the Process Agent of the Borrower in accordance with Paragraph (27) of this Facility Letter.

For and on behalf of  
Changyou.com HK Limited

\_\_\_\_\_  
Name:  
Date:

Witness:



## Exhibit 4.87



恒生銀行  
HANG SENG BANK

理財創富 專注為你  
Managing wealth for you, with you.

Our Ref: Commercial Banking – A130418

Confidential

8 May 2013

Changyou.com HK Limited  
East Tower Jing Yan Building,  
No.29 Shijingshan Road,  
Shijingshan District  
Beijing 100043  
China

Attention: Ms. Jackie Li

Dear Sirs,

## BANKING FACILITIES

**This facility letter supersedes our previous facility letter dated 19 March 2013.**

With reference to our recent discussions, we, Hang Seng Bank Limited (the “**Bank**”) have reviewed your banking facilities and are pleased to offer the following revised banking facility/ facilities (the “**Facilities**”) to the borrower(s) specified below (the “**Borrower**”).

The Facilities will be made available on the terms and conditions set out in this letter and the Standard Terms and Conditions for Banking Facilities attached and upon satisfactory completion of the security specified below.

The Facilities are subject to review at any time and in any event by **31 May 2014** and also subject to our overriding right of repayment on demand, including the right to call for cash cover on demand for prospective and contingent liabilities. The Bank shall have an unrestricted discretion to cancel or suspend, or determine whether or not to permit drawings in relation to, the Facilities.

### 1. Borrower

Changyou.com HK Limited  
Changyou.com Limited

恒生銀行有限公司 Hang Seng Bank Limited  
香港中環德輔道中 83 號 83 Des Voeux Road Central Hong Kong  
電話 Tel (852) 2198 1111  
網址 Website www.hangseng.com

★ 道瓊斯亞太區可持續發展指數成員  
A member of the Dow Jones Sustainability Asia Pacific Index  
★ 富時全球社會責任指數成份股  
A constituent stock of the FTSE4Good Global Index

Member HSBC Group 滙豐集團成員



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Changyou.com HK Limited

Our Ref: Commercial Banking – A130418

**2. Facilities and Limits****(I) Facilities available to Changyou.com HK Limited and Changyou.com Limited (“Borrowing Group I”)**

Term Loan Facility (TL)	USD113,000,000
<b>Total</b>	<b>USD113,000,000</b>

**(II) Facilities available to Changyou.com Limited (“Borrowing Group II”)**

Revolving Loan Facility (RLN)	USD100,000,000
<b>Total</b>	<b>USD100,000,000</b>
<b>Grand Total</b>	<b>USD213,000,000</b>

**3. Facilities and Conditions**

Revolving Loan Facility  
(For Borrowing Group II)

: Facility Amount: USD100,000,000

Drawdown: Drawdown can be made in USD, subject to availability as determined at the Bank's discretion. For any drawdown, Changyou.com Limited shall give the Bank two Business Days prior written notice.

In a minimum amount of USD1,000,000 and an integral multiple of USD500,000.

Drawdown Availability Period: 6 months from the date of this letter.

Final Maturity Date: 1 year from the date of first drawdown.

Interest Rate and Payment: 1.75% per annum over LIBOR or the Bank's Cost of Funds, whichever is higher, payable at the end of each interest period or quarterly in arrears if 6 months period is selected. Changyou.com Limited may select an interest period which shall be 1/2/3/6 months. In any event, no interest period shall beyond the Final Maturity Date.

Repayment: Each loan shall be repayable on the maturity date of such loan drawdown unless the Bank allows for a rollover. In any event, no repayment shall beyond the Final Maturity Date.

2



**Changyou.com HK Limited**  
**Our Ref: Commercial Banking – A130418**

Prepayment: Voluntary prepayment is not permitted during an interest period.

Condition:

- (i) Changyou.com Limited shall maintain deposits and/or Capital Protection Investment product(s) of not less than the outstanding balance of the RLN facility or its equivalent in other currencies placed in Beijing Branch of Hang Seng Bank (China) Limited (the “Deposits”).
- (ii) Changyou.com Limited shall submit to the Bank the payment evidence of the loan purpose within 1 month from the drawdown date of the RLN facility.
- (iii) Changyou.com Limited shall ensure that the Deposits and/or Capital Protection Investment product(s) in name of 北京畅游天下网络技术有限公司 (i.e. or Beijing AmazGame Age Internet Technology Co. Ltd.).
- (iv) The Deposits and/or Capital Protection Investment product(s) can be released subject to this facility fully repaid.

Term Loan Facility  
 (For Borrowing Group I)

: Loan Account No: 337-040802-302

Outstanding Loan Amount: USD113,000,000 as of 2 May 2013

Original Loan Amount: USD150,000,000

Final Maturity Date: 17 September 2013

Interest Rate and Payment: 2.4% per annum over LIBOR or the Bank’s Cost of Funds, whichever is higher, payable at the end of each interest period or quarterly in arrears if 6/12 months period is selected. The Borrower may select an interest period which shall be 1/3/6/12 month(s). No Interest Period shall extend beyond the Final Maturity Date.

Repayment: Principal to be repaid in one lump sum on the Final Maturity Date

All sums which may become due to the Bank from time to time in respect of this facility (including but not limited to principal and interest) are to be directly debited from the account maintained with the Bank.



Changyou.com HK Limited

Our Ref: Commercial Banking – A130418

Prepayment: Prepayment (in whole or in part) is allowed provided that the Bank receives 7 Business Days' prior written notice and such prepayment is made on an interest payment date.

Condition(s):

- (1) The Borrower shall maintain deposits not less than the outstanding balance of the TL facility or its equivalent in other currencies placed in Beijing Branch of Hang Seng Bank (China) Limited (the "Deposits I").
- (2) Submission of legal opinion on the Borrower / guarantor(s) which incorporated overseas (if any) to the Bank.
- (3) The Borrower shall ensure that the Deposits I in name of 北京畅游天下网络技术有限公司 (i.e. or Beijing AmazGame Age Internet Technology Co. Ltd.).
- (4) The Deposits I can be released subject to this facility fully repaid.

4. Security

**The Bank shall continue to hold:-**

For the Borrower

- (1) **Cross Guarantee** dated 5 August 2012 for USD150,000,000 from the Borrower for TL facility only.

5. Undertakings

**The Borrower and the under-mentioned undertaking parties (if any) shall continue to undertake to the Bank as follows:-**

- (1) Changyou.com Limited shall remain its listing status in NASDAQ and its shares shall not be suspended for trading for more than 10 consecutive trading days, unless getting the Bank's consent.
- (2) Changyou.com HK Limited shall remain 100% directly or indirectly owned by Changyou.com Limited.
- (3) The Borrower shall ensure that the depositor 北京畅游天下网络技术有限公司 (i.e. or Beijing AmazGame Age Internet Technology Co. Ltd.) shall be directly or indirectly owned by Changyou.com HK Limited.



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**Changyou.com HK Limited****Our Ref: Commercial Banking – A130418**

- (4) The Borrower undertakes that for any Facilities denominated in Renminbi (if any), it will not directly or indirectly on-lend the proceeds of such Facilities to (i) any individuals and (ii) any Designated Business Customers if the proceeds of such Facilities (or any other Renminbi proceeds derived therefrom) are directly or indirectly credited to Renminbi accounts for the category of Designated Business Customers which are maintained for limited purposes of handling Renminbi cashnotes obtained in their ordinary course of business as Designated Business Customers and for Renminbi bond investment.

“Designated Business Customers” means establishments that have had a business relationship with a Hong Kong Renminbi business participating bank for more than three years which engage in commercial retail, catering, accommodation, transportation services, communications services, medical services, or educational services, including such establishments that have had a business relationship with such participating bank for less than three years, but with concrete evidence to show that they have the actual relevant business background.

The Borrower shall and agree to indemnify the Bank for all losses and liabilities incurred or suffered by the Bank arising out of or in connection with any breach of the above undertaking by the Borrower.

- (5) The Borrower and the corporate guarantor(s) (if any) shall provide to the Bank a certified copy of its annual audited accounts/financial statements within 180 days after the end of each financial year and such other relevant financial information as the Bank may from time to time reasonably request.
- (6) Each of the Borrower and the corporate guarantor(s) (if any) and the corporate security provider(s) (if any) shall immediately inform the Bank once there are changes of its directors or beneficial shareholders or amendment to its memorandum and articles of association or equivalent constitutional documents and shall ensure that such changes/amendment are updated in the company registry of its place of incorporation promptly.

**6. Fees**

Upon completing each review of the Facilities, the Bank is authorised to debit the current account maintained by the Borrower with the Bank for the facility review fee as the Bank may prescribe from time to time.

If applicable, a valuation fee shall be payable by the Borrower for the purpose of valuation of the property by surveyor appointed by the Bank in its sole discretion. The Bank is authorised to debit the current account maintained by the Borrower with the Bank for such valuation fee as the surveyor may charge, notwithstanding that the Borrower does not accept this Facility Letter, the Facilities are not made available due to the Borrower failing to comply with the terms and conditions set out in this Facility Letter, or the Facilities are cancelled or suspended at any time.

5





**Changyou.com HK Limited**  
**Our Ref: Commercial Banking – A130418**

**Section 83 of the Banking Ordinance**

Section 83 of the Banking Ordinance (Cap. 155, Laws of Hong Kong) has imposed on us as a bank certain limitations on advances to persons related to our directors or employees. In accepting the Facilities, the Borrower should advise us whether the Borrower is in any way related to any of our directors or employees within the meaning of Section 83 and in the absence of such advice we will assume that the Borrower is not so related. We would also ask that if the Borrower becomes so related subsequent to accepting the Facilities, the Borrower should immediately advise us in writing.

Please note that in reviewing the application, we may make reference to the credit report(s) of the Borrower(s)/guarantor(s)/security provider(s) (as the case may be) from the credit reference agency(ies). If you wish to access the report(s) yourself, you can contact the credit reference agency(ies) directly at the following address:

Commercial credit reference agency:  
Dun & Bradstreet (HK) Ltd., Unit 1308-1315, 13/F., BEA Tower, Millennium City 5, 418 Kwun Tong Road, Kwun Tong, Kowloon.  
Tel: 2516 1100 ; Fax: 2960 4721.

Please arrange for the enclosed copy of this letter to be signed by the Borrower and all guarantors and security providers of the Facilities and return the same to the Bank with Board Resolution(s) and Shareholder's Resolution(s) (if applicable) of the Borrower and all guarantors and security providers before **8 June 2013**, failing which our offer shall lapse unless it is extended by us at our absolute discretion.

By accepting this Facility Letter, you would agree to channel all your remittance transactions and insurance arrangement to the Bank. Our Cash Management & Payment Services Department and Commercial Sales Department would contact you to offer our services on remittance and insurance respectively.

Should you have any queries, please do not hesitate to contact the following persons:-

Queries on	Name	Telephone No.
Banking arrangement	Ms. Chui Sze Ka Bianca	21985223
Factoring arrangement	Ms. Joan Kwan	21988678
Insurance	Mr. Stanley Ng	36625056
	Mr. John Li	21982522
Remittance	Mr. Billy Chow	21984534
	Remittance Hotline	21986919
Wealth management	Ms. Joey Tsang	21985534
Execution of documents	Documentation Hotline	21982094

Kindly return the accepted Facility Letter and executed documents to **Credit Operations Manager, Credit Operations Department, L21, Tower 2, Enterprise Square V, 38 Wang Chiu Road, Kowloon Bay, Kowloon, Hong Kong.**



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**Changyou.com HK Limited**

**Our Ref: Commercial Banking – A130418**

We trust that you will make active use of the Facilities and are pleased to be of continued assistance.

Yours faithfully,  
For Hang Seng Bank Limited

\_\_\_\_\_  
Jessica Hung  
Senior Vice President  
Portfolio Management and Compliance  
Corporate and Commercial Banking

\_\_\_\_\_  
Jones Chung  
Vice President  
Portfolio Management and Compliance  
Corporate and Commercial Banking

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I/We hereby accept the Facilities and agree to be bound by all the terms and conditions set out in this letter and the Standard Terms and Conditions for Banking Facilities, which I/we have read and understood.

\_\_\_\_\_  
Changyo.com HK Limited

\_\_\_\_\_  
Changyou.com Limited



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**Exhibit 4.88****English Translation**

**Investment Agreement  
Among**

**Koram Games Limited  
(As the Seller)**

**And**

**HEROIC VISION HOLDINGS LIMITED  
(As the Buyer)**

**And**

**Beijing Kunlun Technology Co., Ltd.  
Guangzhou Kunlun Online Information Technology Co., Ltd.  
Kunlun Korea Co., LTD**

**As the Warrantors**

**Signed on November 19, 2013**



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#### Recitals

This Investment Agreement (“this Agreement”) is entered into on November 19, 2013 among and by the following Parties in Beijing, China:

- (1) Koram Games Limited, a limited liability company established and existing under the laws of Hong Kong (registered number: 1415564), with its registered address located at Suite 1203, 12<sup>th</sup> Floor, Ruttonjee House, 11 Duddell Street, Central, HongKong (the “Seller”);
- (2) HEROIC VISION HOLDINGS HOLDINGS, a limited company established and existing under the laws of British Virgin Islands (registered number: 1795916), with its registered address located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (the “Buyer”)
- (3) Beijing Kunlun Technology Co., Ltd., a limited liability company established and existing under Chinese laws (registered number: 110108010907077), with its legal representative as Zhou Yahui, and the registered address located at 605E, Tower B, No. 118 Zhichun Road, Haidian District, Beijing (“Kunlun Beijing”);
- (4) Guangzhou Kunlun Online Information Technology Co., Ltd., a limited liability company established and existing under Chinese laws (registered number: 440106000147934), with its legal representative as Zhou Yahui, and the registered address located at 3F, 44-46 Jianzhong Road, Tianhe District, Guangzhou, Guangdong Province (“Kunlun Guangzhou”);
- (5) Kunlun Korea Co., LTD, a limited company established and existing under the Korean laws (registered number: 2148870398). with its registered address located at 10F823Bldg, 823-16 Yeoksam-Dong, Gang-nam Gu (“Kunlun Korea”).

The above Parties are called collectively as the “Parties” and respectively as a “Party”. The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea are called collectively as “Warrantors” and respectively as a “Warrantor”.

#### WHEREAS,

- (1) From the Signature Date on, the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea hold the target asset and run RaidCall voice service and other related businesses of each Warrantor (“Target Business”). Target asset refers to all assets required by the operation of the Target Business, including all the tangible or intangible assets, real estate or private properties, employees and qualifications held, owned or controlled by each Warrantor that are to be transferred to the Hong Kong company according to Article 3.3.1, and including all the assets and employees listed in Annex 4 as well as the additions, changes or modifications agreed in writing by the Buyer and the Seller from time to time. The Seller, Kunlun Guangzhou and Kunlun Korea are subsidiaries wholly owned by Kunlun Beijing.
- (2) The Seller shall, in five (5) business days upon the conclusion of this Agreement, set up a limited company (“Target Company”) in British Virgin Islands according to the laws thereof, the equity structure of which shall follow the below structure at its establishment:

Category	Authorized Stock	Share Issued	Face Value	Shareholder
Ordinary Share	USD 50,000	7,500	USD1.00 per share	Seller



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- (3) The Buyer intends to, according to this Agreement
  - (i) Buy from the Seller, and the Seller agrees to transfer 3,750 ordinary shares of the Target Company it held ("Seller Shares") to the Buyer; and
  - (ii) Subscribe from the Target Company, and the Target Company agrees to issue 2,500 ordinary shares ("Shares to be Subscribed") to the Buyer.
- (4) After closing (the Payment Date of the Remaining Consideration included), the Buyer will hold 62.5% shares of the Target Company (fully diluted).
- (5) The Parties agree that, after the procedures of the reorganization plan are completed,
  - (i) The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea have transferred the Target Business in the Hong Kong company and WFOE to enable the Hong Kong company to run the Target Business only with the target assets after the closing in the same form and scale with the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea operated prior to the Closing Date.
  - (ii) The Target Company holds 100% stock rights of the Hong Kong company; and
  - (iii) The Hong Kong company holds 100% stock rights of WFOE.

The Parties therefore reach the following agreement as to the transaction hereunder on the basis of equality and negotiation:

## **Article 1 Definitions and Interpretation**

### **1.1 Definitions**

Unless otherwise specified in the context, the terms herein in bold shall have the meaning with those listed in Annex 1.

### **1.2 Interpretation**

- 1.2.1 Any reference to the Agreement includes annexes and appendixes that are inseparable from the Agreement. "Hereof", "hereunder", "herein" and other words with similar meanings shall refer to the entire Agreement other than some article, schedule, annex or appendix. Any reference to any document (including the Agreement) shall be interpreted as the document amended, consolidated, supplemented, updated or superseded from time to time. Unless otherwise specified, (i) any annex or appendix mentioned shall refer to corresponding annex or appendix hereto, and (ii) any article mentioned shall refer to corresponding article in the main body of the Agreement.
- 1.2.2 "Including" used herein shall be interpreted as "including but not limited".
- 1.2.3 Any reference to any Party to the Agreement or any other agreement or document shall be interpreted as including such Party's successor or authorized transferee.
- 1.2.4 "Person" shall include natural person, business office, company, government authority, joint operational project, partnership, committee, unincorporated organization, trust, corporation or other entity (regardless of independent legal entity status).





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## Article 2 Subscription and Acceptance of Ordinary shares

### 2.1 Accept Seller Shares

Subject to the terms and conditions of this Agreement and dependent upon the representations and warranties of this Agreement and other transaction documents, the Seller agrees to sell and transfer to the Buyer, and the Buyer agrees to purchase and accept the Seller Shares from the Seller.

### 2.2 Subscribe the Shares to be Subscribed

Subject to the terms and conditions of this Agreement and dependent upon the representations and warranties of this Agreement and other transaction documents, the Target Company agrees to issue to the Buyer, and the Buyer agrees to subscribe the shares to be subscribed from the Target Company.

### 2.3 Consideration and Payment

2.3.1 The Buyer shall pay the Seller a total consideration of USD 30,000,000 or equivalent RMB amount deducting the accounts payable ("Transfer Consideration") for the shares to be transferred. The Buyer shall, on the Closing Date and through bank transfer, transfer USD 10,000,000 or equivalent amount of RMB (determined according to the middle rate of the exchange rate of USD against RMB published by the People's Bank of China on its official website on the fifth (5<sup>th</sup>) business day before the Closing Date) to the trust account designated jointly by the Seller and the Buyer at least three (3) business days prior to the Closing Date in writing (the "Initial Transfer Consideration"). The Buyer shall, on the Payment Date of the Remaining Consideration and through bank transfer, transfer USD 20,000,000 or equivalent amount of RMB deducting accounts payable (determined according to the middle rate of the exchange rate of USD against RMB published by the People's Bank of China on its official website on the fifth (5<sup>th</sup>) business day before the Payment Date of the Remaining Consideration) to the account designated at least three (3) business days prior to the Payment Date of the Remaining Consideration in writing ("the Remaining Transfer Consideration"). The Initial Transfer Consideration in the trust account shall be transferred to such account designated by the Seller at the same time on the Payment Date of the Remaining Consideration.

2.3.2 The Buyer shall pay the Target Company a total consideration of USD 20,000,000 (or equivalent RMB amount) as the subscription consideration for the Shares to be Subscribed. The Buyer shall, on the Closing Date and through bank transfer, transfer USD 1 or equivalent amount of RMB (determined according to the middle rate of the exchange rate of USD against RMB published by the People's Bank of China on its official website on the fifth (5<sup>th</sup>) business day before the Closing Date) to the account designated by the Target Company at least three (3) business days prior to the Closing Date in writing, and shall, on the Payment Date of the Remaining Consideration and through bank transfer, transfer USD 19,999,999 or equivalent amount of RMB (determined according to the middle rate of the exchange rate of USD against RMB published by the People's Bank of China on its official website on the fifth (5<sup>th</sup>) business day before the Closing Date) to the account designated by the Target Company at least three (3) business days prior to the Payment Date of the Remaining Consideration in writing ("the Remaining Subscription Consideration").



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### Article 3 Prerequisite

#### 3.1 Prerequisite for the Buyer to Agree to Close

The Buyer agrees to close on the premise that each Warrantor shall, and shall make every reasonable effort to, urge other Parties to fulfill the conditions of this article on or before the Closing Date, and such fulfillment shall be to the satisfaction of the Buyer, unless such fulfillment is exempted by the Buyer in writing (fully exempted or partly exempted by additional exemption conditions).

- 3.1.1 The legally establishment and valid existence of the Target Company: the Seller has acquired all permissions, certificates and certifications proving the legally establishment and valid existence of the Target Company, and has provided reasonable satisfactory evidence to the Buyer to demonstrate that it is duly organized and validly existing.
- 3.1.2 Confirmatory due diligence: The due diligence result of various aspects (including business, technology, finance and law) of Target Business, target asset and target group and others shall be to the satisfaction of the Buyer, or all major issues of such due diligence have been remedied by each Warrantor with the method that the Buyer is satisfied.
- 3.1.3 Closing warranty and the warranty on the Target Business and target asset made by each Warrantor are accurate: All the closing warranties each Warrantor made in Part I of Annex 2 and all the warranties made in relation with the Target Business and target asset in Part III of Annex 2 are, on the date of this Agreement (if related to the Target Company, the establishment date of the Target Company shall prevail) and every single day before the Closing Date (included), real, accurate and intact in all aspects as if such closing warranties are made on such every single day.
- 3.1.4 Representations and warranties made by each Warrantor are accurate: All the representations and warranties each Warrantor made in Part IV of Annex 2 are, on the date of this Agreement and every single day before the Closing Date (included), real, accurate and intact in all aspects as if such closing warranties are made on such every single day.
- 3.1.5 Fulfillment: The Seller and each Warrantor have fulfilled and followed all the agreements, commitments, obligations and conditions included in each transaction document that they should have been fulfilled or followed on or before the closing, including the conditions listed in this Article 3.1 and the commitments listed in Articles 4 and 7.
- 3.1.6 Delivery of closing document: The Seller and the Target Company have fulfilled their obligations at closing on or before the Closing Date according to Articles 5.2 and 5.3.
- 3.1.7 Consent: All the consent required for the transaction (including the approval from competent government departments) shall have been obtained (no condition unacceptable by the Buyer has been added) and remain fully valid.
- 3.1.8 Company procedures: The board of directors and Shareholders' Meeting of the Seller and the Target Company shall pass necessary resolutions to approve the proposed transaction under the transaction document, and approve the conclusion, delivery and performance of each transaction document to which it is a party.
- 3.1.9 No material adverse effect: There is no event that will impose material adverse effect on the Target Business, target asset and the Target Company.
- 3.1.10 No adverse procedure: There is no person that threatens to raise or has raised an appeal or pending appeal that (1) tries to limit, prevent or seriously influence each Warrantor to own or manage all or any major part of its business or asset (including Target Business or target asset), or forces each Warrantor to dispose all or any major part of its business or asset, or (2) tries to exert or confirm limit on the fulfillment of the transaction or the capacity of the Seller to validly exercise its ownership over the stock rights of the Target Company, and forces it to dispose any part of its stock rights in the Target Company.



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- 3.1.11 No adverse law change: There is no appeal raised by any government department or any change that is suggested, promulgated, implemented, released, or issued by any government department, or to any applicable law deemed applicable to the transaction or the interpretation of existing law, and such change, through reasonable judgment, will directly or indirectly restrict the fulfillment of the transaction in major aspects or lead to any consequence mentioned in Article 3.1.10
- 3.1.12 Director, legal representative and supervisor: The Target Company shall have only two (2) directors, and the remaining directors shall have respectively submitted their written resignation letter and the commitment letter signed by them stating their waiver of all rights and claims on the Target Company, and such resignation letter and commitment letter shall become effective as of the Closing Date. The three (3) personnel designated by the Buyer have been properly appointed as directors of the Target Company and such appointment shall become effective as of the Closing Date, and such new directors have submitted required registration to relevant department of British Virgin Islands for the record properly.
- 3.1.13 Bank account and signatory: The signatory of the Target Company for the present bank account (if any) shall have been dismissed, and a new signatory nominated by the Buyer shall have been appointed properly for the bank account owned by the Target Company on the Closing Date.
- 3.1.14 Articles of Association of the Target Company: The Target Company shall have passed the amended and restated Articles of Association of the Target Company with the format and content satisfied by the Buyer ("Articles of Association of the Target Company")
- 3.1.15 Relevant registration proxy of the Target Company: The contact in charge of contacting relevant registration proxy of the Target Company has been changed to the personnel designated by the Buyer.
- 3.2 Prerequisite for each Warrantor to Agree to Close
- Each Warrantor agrees to close on the premise that the Buyer shall be able to fulfill the conditions of this Article on or before the Closing Date, and such fulfillment shall be to the satisfaction of the Seller, unless such fulfillment is exempted by the Seller in writing (fully exempted or partly exempted by additional exemption conditions).
- 3.2.1 Warranties made by the Buyer are accurate: All the warranties the Buyer made in Part V of Annex 2 are, on the date of this Agreement and every single day before the Closing Date (included), real, accurate and intact in all aspects as if such Buyer warranties are made on such every single day.
- 3.2.2 Fulfillment: The Buyer has fulfilled and followed all the agreements, commitments, obligations and conditions included in each transaction document that it should have been fulfilled or followed on or before the closing, including the conditions listed in this Article 3.2.
- 3.2.3 Closing document: The Buyer has provided all closing documents on or before the Closing Date according to Article 5.4.
- 3.2.4 Consent: All the consent required for the transaction (including the approval from competent government departments) shall have been obtained (no condition unacceptable by the Seller has been added) and remain fully valid.



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3.3 Prerequisite for the Buyer to Agree to Pay the Remaining Consideration

The Buyer agrees to pay the remaining consideration on the premise that each Warrantor shall, and shall make every reasonable effort to, urge other Parties to fulfil the conditions of this Article on or before the Payment Date of the Remaining Consideration, and such fulfillment shall be to the satisfaction of the Buyer, unless such fulfillment is exempted by the Buyer in writing (fully exempted or partly exempted by additional exemption conditions).

3.3.1 Complete the reorganization plan procedures:

- (a) Each Warrantor has already completed the procedures listed in the reorganization plan and has provided proof to the Buyer to its satisfaction, including transfer of Target Business to the Hong Kong company and WFOE without any encumbrance and the target asset, permission, certificates and certifications (including those listed in Annex 7) required by or related to all the Target Business held, owned or controlled by each Warrantor, in which: (i) the staffs of the Target Business have terminated their labor contracts properly with the Seller, Kunlun Beijing, Kunlun Guangzhou or Kunlun Korea, and quitted all charges related to the termination of labor relationship (including indemnification) under the condition that the length of service is calculated continuously, and shall sign new labor contracts, confidentiality agreement and non-competition agreement with the Hong Kong company or WFOE; (ii) a tripartite agreement has been signed by the relevant parties of the Original Contract, the Seller and the Hong Kong company on the transfer of relevant rights and obligations for the business contract in the target asset; (iii) the registration of software copyright and domain name in the target asset has been transferred to Hong Kong company or WFOE.
- (b) The Hong Kong company and WFOE has obtained all permissions, certificates and certifications to prove that the procedures in the reorganization plan has been completed, and has provided evidence to the Buyer to its satisfaction proving that the Hong Kong company and WFOE can run the Target Business with the target assets in the same form and scale with the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea operated prior to the Payment Date of Remaining Consideration, including the permissions, certificates and certifications set forth in Annex 7.

3.3.2 Confirmatory due diligence: The due diligence result of various aspects (including business, technology, finance and law) of Target Business, target asset and target group and others shall be to the satisfaction of the Buyer, or all major issues of such due diligence have been remedied by each Warrantor with the method that the Buyer is satisfied.

3.3.3 Warranties on the payment of the remaining consideration are accurate: All the warranties on the payment of the remaining consideration each Warrantor made in Part II of Annex 2 and all the warranties made in relation with the Target Business and target asset in Part III of Annex 2 are, on the date of this Agreement and every single day before the Payment Date of the Remaining Consideration (included), real, accurate and intact in all aspects as if such warranties on the payment of the remaining consideration are made on such every single day.

3.3.4 Representations and warranties made by each Warrantor are accurate: All the representations and warranties each Warrantor made in Part IV of Annex 2 are, on the date of this Agreement and every single day before the Payment Date of the Remaining Consideration (included), real, accurate and intact in all aspects as if such representations and warranties are made on such every single day.

3.3.5 Fulfillment: The Seller and each Warrantor have fulfilled and followed all the agreements, commitments, obligations and conditions included in each transaction document that they should have fulfilled or followed on or before the payment of the remaining consideration, including the conditions listed in this Article 3.3 and the commitments listed in Articles 4 and 7.



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- 3.3.6 Deliver the remaining consideration payment document: The Seller and the Target Company have fulfilled their obligations at the payment of the remaining consideration on or before the Payment Date of the Remaining Consideration according to Articles 5.6 and 5.7.
- 3.3.7 Consent: All the consent required for the transaction (including the approval from competent government departments) shall have been obtained (no condition unacceptable by the Buyer has been added) and remain fully valid.
- 3.3.8 Company procedures: The board of directors and shareholders', meeting of each Warrantor shall pass necessary resolutions to approve the proposed transaction under the reorganization plan to which it is a party;
- 3.3.9 No material adverse effect: There is no event that will impose material adverse effect on the Target Business, target asset and the Target Group.
- 3.3.10 No adverse procedure: There is no person that threatens to raise or has raised an appeal or pending appeal that (1) tries to limit, prevent or seriously influence each Warrantor to own or manage all or any major part of its business or asset (including Target Business or target asset), or forces each Warrantor to dispose all or any major part of its business or asset, or (2) tries to exert or confirm limit on the fulfillment of the transaction or the capacity of the Seller to validly exercise its ownership over the stock rights of the Target Company, and forces it to dispose any part of its stock rights in the Target Company.
- 3.3.11 No adverse law change: There is no appeal raised by any government department or any change that is suggested, promulgated, implemented, released, or issued by any government department, or to any applicable law deemed applicable to the transaction or the interpretation of existing law, and such change, through reasonable judgment, will directly or indirectly restrict the fulfillment of the transaction in major aspects or lead to any consequence mentioned in Article 3.3.10
- 3.3.12 Director, legal representative and supervisor: The three (3) directors of Hong Kong company and the present legal representative of WFOE, the three (3) directors and the only supervisor should have been appointed properly as the designated personnel of the Buyer, and such legal representative, directors and supervisor have been registered with Hong Kong Companies Registry and competent industrial and commercial department of China for the record.
- 3.3.13 Bank account and signatory: Personnel nominated by the Buyer shall have been appointed as the signatory of the present bank account (if any) of the Hong Kong company and WFOE, and relevant E-bank key has been handed over to such personnel.
- 3.3.14 Articles of Association: The Hong Kong company and WFOE shall have passed an Articles of Association of the Hong Kong company and WFOE with the format and content satisfied by the Buyer (collectively as "Articles of Association of Each Group" together with the above "Articles of Association of the Target Company").
- 3.3.15 Labor contract, confidentiality agreement and non-competition agreement: The Hong Kong company or WFOE shall sign labor contract, confidentiality agreement and non-competition agreement with each staff of the Target Business. If the employees of the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea engaging in the work related to the Target Business are not included in the target asset before restructuring, they shall have signed proper confidentiality agreement and non-competition agreement with the Seller, Kunlun Beijing, Kunlun Guangzhou, Kunlun Korea and the Target Company to ensure that they will keep the information related to the Target Business confidential and that they will not engage in any business identical or similar with the Target Business.



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- 3.3.16 Relevant registration proxy of the Hong Kong company and WFOE: The contact in charge of contacting relevant registration proxy of the Hong Kong company and WFOE has been changed to the personnel designated by the Buyer.
- 3.3.17 Information technology, registered player information and history operation data: The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea shall have handed all the information technology of the Target Business (including but not limited to the software under development), registered player information, history operation data and code backup over to the Target Company and have deleted them so that no backup is left.
- 3.3.18 Business cooperation agreement: Taiwan Molly Digit Marketing Co., Ltd. has signed a business cooperation agreement with the Hong Kong company.

3.4 Best Reasonable Effort

The Buyer and each Warrantor shall cooperate with each other to, with their best reasonable effort, adopt or urge other Parties to adopt necessary, proper or wise actions to accomplish the proposed transaction hereunder according to this Agreement and applicable laws (including completing the closing and the remaining consideration payment conditions to be completed by them under Articles 3.1 to 3.3, and obtaining or delivering the closing and the remaining consideration payment documents listed in Articles 5.2 to 5.7), including to prepare and submit all documents as soon as possible to finish all necessary notices, reports, submissions and other records, and to obtain all the consent required to accomplish the proposed transaction hereunder as soon as possible.

**Article 4 Promises of each Warrantor prior to the Closing and the payment of the remaining consideration**

4.1 Promises of each Warrantor prior to the Closing

- 4.1.1 Limitation of activities: Unless agreed in writing by the Buyer and required for the completion of proposed transactions hereunder or under other transaction documents or otherwise provided herein, each Warrantor warrants to the Buyer individually and jointly that:
- (a) The Seller and each Warrantor will not exercise its shareholder's rights of the Target Company prior to the Closing or perform any act which may affect the assessment or value of stock rights of the target group or Target Business and relevant business as well as target assets, including the conclusion of any agreement or promise which may result in encumbrances on any share or Target Business and relevant business of the Target Company and target assets held by the Seller;
  - (b) Prior to the Closing, the Target Company will not:
    - (i) Amend its organizational documents;
    - (ii) Change the management structure of the Company;
    - (iii) Change its capital or declare, withdraw or pay any dividend or make other assignment in connection with its securities (whether in cash, share, property or its portfolios), or redeem, repurchase or acquire any security in any other manner, or propose an offer to redeem, repurchase or acquire any security in any other manner;
    - (iv) (1) Issue, pay or sell, or authorize the issuance, payment or sale of any security, or (2) Modify any term of any security (whether by merger, acquisition or otherwise);
    - (v) Exist any capital expenditure, obligation or responsibility with respect to an amount exceeding RMB 300,000 in a transaction or a series of similar or relevant transactions;
    - (vi) Directly or indirectly acquire any asset, security, property, interest or business (whether by merger, consolidation, equity or assets acquisition or otherwise);





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- (vii) Sell, lease or otherwise assign its any asset, security, property, interest or business, or create or incur any encumbrance on it;
- (viii) Provide any loan, advance payment or capital contribution to any other person, or invest in such person (excluding any advance payment in normal business activities);
- (ix) Create, incur or undertake any borrowing or security; allow the existence of any borrowing or security or otherwise assume responsibility for any borrowing or security;
- (x) Conclude any agreement or make any promise on any assignment of intellectual property rights to a third party, or any approval of the use of intellectual property rights by a third party;
- (xi) Change accounting policies or methods, except its auditor agrees that it is required by the simultaneous change of any US Generally Accepted Accounting Principles or China Generally Accepted Accounting Principles;
- (xii) Reconcile, put forward or propose reconciliation in connection with the following matters: (1) any action, inquiry, arbitration, procedure or other claims involved in or against Target Business and target assets; or (2) any action, arbitration, procedure or dispute related to the proposed transaction herein;
- (xiii) Make or change any tax election, change any annual tax accounting period, adopt or change any tax accounting method, modify any tax declaration or submit the request for tax refund, reach any settlement agreement, reach a compromise on the claim for reimbursement, audit or assessment of tax, waive any tax refund, set off or otherwise cut the right of claim for tax obligations (unless agreed by the Buyer); or
- (xiv) Agree, resolve or promise to perform any of the above-mentioned acts.

4.1.2 Complete the conditions precedent to the Closing: each Warrantor shall use all its reasonable endeavors to cause the completion of conditions precedent to the Closing as agreed in Article 3.1, including (1) take actions necessary to ensure the execution, delivery and performance of documents concerning any precedent condition to which each Warrantor is a party; and (ii) cause each Warrantor to adopt the shareholders resolutions and board resolutions, so as to approve the transactions described herein (including the reorganization plan), and amend and/or adopt the Articles of Association of the Target Company and all relevant transaction documents.

4.1.3 Trademark: each Warrantor shall employ its best efforts to cause the Hong Kong company or WFOE to submit an application for the registration of the word Raidcall and graphic LOGO trademark to the competent authority for trademark registration, and the Buyer agrees to employ its reasonable efforts to assist the Hong Kong company or WFOE in the submission of such application. If the Hong Kong company or WFOE fails to submit such application prior to the Closing or the payment of the remaining consideration, each Warrantor promises to ensure that the Hong Kong company or WFOE will submit such application after the payment of the remaining consideration.





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- 4.2 Promises of each Warrantor prior to the payment of the remaining consideration
- 4.2.1 Conduct the Target Business as usual: from the date of signing to the date of payment of the remaining consideration, except as required by the reorganization plan or transactions, each Warrantor undertakes with the Buyer individually and jointly that it will: (i) continue the operation of Target Business in the same form and scale as those of previous operation and abide by all the contracts which it concluded with respect to the Target Business and target assets and applicable laws; (ii) keep the completeness of existing operating organization of group companies; (iii) ensure the validity of consents of government authority in the place where all its Target Business and target assets are operated and obtain any consent not obtained and necessary for group companies to conduct the Target Business; (iv) ensure that the group companies pay all due debts or taxes; (v) maintain the target assets in current scale; (vi) with respect to the Target Business, maintain the provision of service by the management personnel and employees; (vii) with respect to the Target Business, maintain good relations with relevant consumers, show host, distributors, suppliers of the server and bandwidth and other parties with which it has major business relationships, and maintain the continuity of target targets, without disruption of services due to the transfer of contracts or change in the server; and (viii) with respect to the Target Business, keep the books and records relating to it in the manner consistent with the previous one.
- 4.2.2 Limitation of activities: Without limiting the foregoing Article 4.2.1, unless agreed in writing by the Buyer and required for the completion of proposed transactions hereunder or under other transaction documents or otherwise provided herein, each Warrantor warrants to the Buyer individually and jointly that the Seller and each Warrantors will not perform any act in any manner which may affect the Target Business and relevant business as well as target assets prior to the payment of the remaining consideration, including the conclusion of any agreement or promise which may result in encumbrances on any Target Business, relevant business and target assets, and any act of disposition of target assets (except as required during normal business process).
- 4.2.3 The debts of Target Business and target assets prior to the completion of reorganization plan: each Warrantor warrants to the Buyer that the relevant responsibilities prior to the assignment of Target Business and target assets to relevant group companies in accordance with the reorganization plan (including any debt, potential tax burden, potential responsibility to pay the social insurance and housing fund or other responsibilities) will not be transferred to the group companies but be undertaken by the Seller, Kunlun Beijing, Kunlun Guangzhou or Kunlun Korea.
- 4.2.4 Assist in the confirmatory due diligence: each Warrantor shall use all its reasonable endeavors to assist the Purchaser in conducting and completing the confirmatory due diligence.
- 4.2.5 Complete the reorganization plan: each Warrantor shall use all its reasonable endeavors to assist and promote the completion of and complete the procedures listed in the reorganization plan.
- 4.2.6 Complete the conditions precedent to the payment of the remaining consideration: each Warrantor shall use all its reasonable endeavors to cause the completion of conditions precedent to the payment of the remaining consideration as agreed in Article 3.3, including (1) take actions necessary to ensure the execution, delivery and performance of documents concerning any precedent condition to which each Warrantor is a party; and (ii) cause each Warrantor to adopt the shareholders resolutions and board resolutions, so as to approve the transactions described herein (including the reorganization plan), and amend and/or adopt the articles of association of the groups and all relevant transaction documents.
- 4.2.7 Intangible assets: introduce three software under research and development in the target assets, store them in the research and development server, conduct trial operation prior to the Closing and backup them to a hard disk.



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## Article 5 Closing

### 5.1 Closing

The Closing shall be carried out within five (5) business days upon the satisfaction or exemption of all precedent conditions listed in Article 3.1 and 3.2 in Beijing, China, or at any other time, on any other date or in any other place otherwise jointly agreed in writing by the Seller and the Buyer ("Closing Date").

### 5.2 Obligations of the Seller at the Closing

The Seller shall or causes other parties to deliver the originals of the following documents to the Buyer at or prior to the Closing (unless otherwise specified below):

- 5.2.1 The instrument of transfer duly signed by the Seller on the transfer of the Seller Shares to the Buyer;
- 5.2.2 The share certificate on the Seller Shares held by the Seller, to be forwarded to the Target Company for deregistration;
- 5.2.3 The certificate signed by the authorized representative of the Seller with the date being the Closing Date (the contents of which shall be reasonably satisfactory to the Buyer), with the precedent conditions listed in Article 3.1 confirmed to have been satisfied;
- 5.2.4 The Shareholder Agreement duly signed by the Seller;
- 5.2.5 The copies of shareholders resolutions and board resolutions of the Seller required for the Seller's conclusion of this Agreement and transaction documents and completion of proposed transactions under transaction documents, including the consent and approval to (i) execute all transaction documents; (ii) sell the Seller Shares; (iii) issue the shares to be subscribed; (iv) allow the rest of directors in excess of two (2) ones to resign position in the Target Company; (v) assign three (3) appointed persons of the Buyer to serve as directors of the Target Company; (vi) revoke the signatory of current bank account (if any) of the Target Company, and with respect to the bank account owned by the Target Company on the Closing Date, assign a new signatory of bank account nominated by the Buyer; (vii) accept the copy of Articles of Association of the Target Company, the authenticity and completeness of which shall be certified by a director of the Seller; and
- 5.2.6 The supporting documents proving that the personnel of the Seller signing this Agreement have been duly authorized and are entitled to sign this Agreement on behalf of the Seller, including the resolutions of the shareholders' meeting and/or board of directors issued by the Seller with respect to such authorization.

### 5.3 Obligations of each Warrantor at the Closing

Each Warrantor shall or causes the Target Company or other parties to deliver the originals of the following documents to the Buyer at or prior to the Closing (unless otherwise specified below).

- 5.3.1 The share certificates duly signed and issued by the Target Company on the Seller Shares and shares to be subscribed under the Purchaser's name;
- 5.3.2 The copy of register of shareholders certified by the company secretary of the Target Company, indicating that the Buyer has become the shareholder of the Seller Shares and Shares to be Subscribed;
- 5.3.3 The certificate signed by the authorized representative of each Warrantor with the date being the Closing Date (the contents of which shall be reasonably satisfactory to the Buyer), with the precedent conditions listed in Article 3.1 confirmed to have been satisfied;
- 5.3.4 The Shareholder Agreement duly signed by the Target Company;
- 5.3.5 Other transaction documents duly signed by each Warrantor and other documents required for the completion of proposed transactions under transaction documents (the contents and form of which shall be reasonably satisfactory to the Buyer);



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- 5.3.6 Evidence reasonably satisfactory to the Buyer, to prove that the Target Company has adopted the articles of association;
- 5.3.7 The supporting document proving that the Target Company has properly filed with relevant departments of British Virgin Islands corresponding changes in the registration particulars of the articles of association of Target Company and registered for the record as required by the relevant registration agent of Target Company (such supporting document may be sent by the registration agent of Target Company by e-mail);
- 5.3.8 The copies of resolutions of shareholders' meeting and board of directors of each Warrantor (excluding the Seller) required for each Warrantor's (excluding the Seller) conclusion of this Agreement and transaction documents and completion of proposed transactions under transaction documents (including the consent and approval to execute all relevant transaction documents), the authenticity and completeness of which shall be certified by a director of each Warrantor;
- 5.3.9 The written resignation letters and commitment letters duly signed on a waiver of all claims against the Target Company from the rest of directors in excess of two (2) directors effective on the Closing Date of the Target Company;
- 5.3.10 The supporting document proving that the personnel of each Warrantor signing this Agreement have been duly authorized by each Warrantor and are entitled to sign this Agreement on behalf of each Warrantor, including the resolutions of the shareholder's meeting and board of directors issued by each Warrantor with respect to such authorization.
- 5.3.11 The official seal, financial seal and contract seal of the Target Company and other seals representing the Target Company;
- 5.3.12 All the company's books, registers of shareholders and directors, articles of association, certificate of incorporation, accounting records and other records of the Target Company since its establishment, including without limitation to check books, labor contracts, all historical files and payroll records, social welfare and insurance settlement, capital verification reports, resolutions and minutes of the shareholders' meeting and board of directors, and all government approval documents, certificates, licenses and notices; the authenticity and completeness of such books and records shall be certified by a director of the Target Company, and it shall be acknowledged and confirmed that all such books and records of the Target Company are restored in the registration address of the Target Company;
- 5.3.13 With respect to the bank account owned by the Target Company on the Closing Date, the record demonstrating that the new signatory of bank account nominated by the Buyer has obtained the signature card of the bank account properly appointed;
- 5.3.14 The contact person responsible for contacting the relevant registration agent of the Target Company has been changed to a person appointed by the Buyer; and
- 5.3.15 The certificates and licenses listed in Annex 7 and other certificates and licenses set forth in accordance with Article 3.1.1.
- 5.4 Obligations of the Buyer at the Closing  
At or prior to the Closing, the Buyer shall:
  - 5.4.1 Transfer the Initial Transfer Consideration into the escrow account in accordance with the provisions of Article 2.3.1;
  - 5.4.2 Pay the Target Company USD 1 or equivalent RMB in accordance with the provisions of Article 2.3.2;
  - 5.4.3 Deliver the Shareholder Agreement duly signed by the Buyer;



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- 5.4.4 Deliver the certificate signed by the authorized representative of the Buyer with the date being the Closing Date (the contents of which shall be reasonably satisfactory to the Seller), with the precedent conditions listed in Article 3.2 confirmed to have been satisfied; and
- 5.4.5 The copies of shareholders resolutions and board resolutions of the Buyer required for the Buyer's conclusion of this Agreement and transaction documents and completion of proposed transactions under transaction documents, the authenticity and completeness of which shall be certified by a director of the Buyer;
- 5.5 Payment of the remaining consideration  
The payment of the remaining consideration shall be carried out within five (5) business days upon the satisfaction or exemption of all precedent conditions listed in Article 3.3 in Beijing, China, or at any other time, on any other date or in any other place otherwise jointly agreed in writing by the Seller and the Buyer ("Payment Date of the Remaining Consideration").
- 5.6 Obligations of the Seller at the payment of the remaining consideration  
The Seller shall or causes other parties to deliver the originals of the following documents to the Buyer at or prior to the payment of the remaining consideration (unless otherwise specified below):
  - 5.6.1 The certificate signed by the authorized representative of the Seller with the date being the Payment Date of the Remaining Consideration (the contents of which shall be reasonably satisfactory to the Buyer), with the precedent conditions listed in Article 3.3 confirmed to have been satisfied;
- 5.7 Obligations of each Warrantor at the payment of the remaining consideration  
Each Warrantor shall cause the group companies or other parties to deliver the originals of the following documents to the Buyer at or prior to the payment of the remaining consideration (unless otherwise specified below):
  - 5.7.1 The certificate signed by the authorized representative of each Warrantor with the date being the Payment Date of the Remaining Consideration (the contents of which shall be reasonably satisfactory to the Buyer), with the precedent conditions listed in Article 3.3 confirmed to have been satisfied;
  - 5.7.2 The documents duly signed by each Warrantor and required for the completion of proposed transactions under transaction documents (including the reorganization plan) (the contents and form of which shall be reasonably satisfactory to the Buyer);
  - 5.7.3 Provide the evidence reasonably satisfactory to the Buyer, to prove that the Hong Kong company and WFOE have adopted their articles of association, applied for approval of and/or registration for such articles of association with the Companies Registry in Hong Kong, China's competent administrative department for industry and commerce and China's commercial administrative department, and carried out registration procedures for the record as required by relevant registration agent;
  - 5.7.4 The resolutions of shareholders' meeting and board of directors of each Warrantor (excluding the Seller) required for each Warrantor's (excluding the Seller) completion of proposed transactions under transaction documents (including the consent and approval);
  - 5.7.5 The official seal, financial seal and contract seal of the Hong Kong company and WFOE and other seals representing the Hong Kong company and WFOE;
  - 5.7.6 The certificates and licenses listed in Annex 7 and other certificates and licenses set forth in accordance with Article 3.3.1;
  - 5.7.7 The list of relevant assigned target assets received by the Hong Kong company on or prior to the Payment Date of the Remaining Consideration (the contents of which shall be reasonably satisfactory to the Buyer);



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- 5.7.8 The list of relevant assigned target assets received by WFOE on or prior to the Payment Date of the Remaining Consideration (the contents of which shall be reasonably satisfactory to the Buyer); and
- 5.7.9 The confirmation letter signed by the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea, confirming that the backup of all the information technologies related to the Target Business (including without limitation to the software still under development), information of registered players, historical operational data and code have been given to the Target Company and deleted and there exists no backup.
- 5.8 Obligations of the Buyer at the payment of the remaining consideration  
At or prior to the payment of the remaining consideration, the Buyer shall:
  - 5.8.1 Pay the remaining transfer consideration in accordance with the provisions of Article 2.3.1;
  - 5.8.2 Agree to transfer the Initial Transfer Consideration in the escrow account into the account designated by the Seller in accordance with the provisions of Article 2.3.1; and
  - 5.8.3 Pay the Remaining Subscription Consideration to the Target Company in accordance with the provisions of Article 2.3.2.
- 5.9 Delivery upon the Closing  
Within the following time limit upon the Closing, each Warrantor shall or causes other parties to deliver the originals of the following documents reasonably satisfactory to the Buyer (unless otherwise specified below):
  - 5.9.1 Within three (3) business days upon the Closing, update in accordance with the laws of British Virgin Islands and submit the register of shareholders of Target Company registering corresponding changes in the registration particular to relevant departments of British Virgin Islands;
  - 5.9.2 Within three (3) business days upon the Closing, update in accordance with the laws of British Virgin Islands and submit the director list of Target Company registering corresponding changes in the registration particular to relevant departments of British Virgin Islands;
  - 5.9.3 Within three (3) business days upon the Closing, update in accordance with the laws of British Virgin Islands and submit the articles of association of Target Company registering corresponding changes in the registration particular to relevant departments of British Virgin Islands;
  - 5.9.4 Within twenty (20) business days upon the Closing and prior to the Payment Date of the Remaining Consideration, each Warrantor shall or causes other parties to deliver the supporting document reasonably satisfactory to the Buyer and enough to prove that the establishment of Target Company has been registered with the China's commercial administrative department and foreign exchange administrative department for the record.
- 5.10 Obligations after the payment of the remaining consideration
  - 5.10.1 After the payment of the remaining consideration and prior to the establishment of an entity for completing the operation of Target Business by the target group in Taiwan, Kunlun Beijing shall cause Taiwan Molly Digit Marketing Co., Ltd. and the Hong Kong company to conclude a business cooperation agreement and Taiwan Molly Digit Marketing Co., Ltd. to continue to operate the Target Business in Taiwan, so as to ensure that all the services of Target Business in Taiwan can be operated as usual (including negotiating with the local Copyright Society with respect to the authorization of copyrights to songs in Taiwan), and transfer the income from the Target Business into the account designated by the target group for free. The specific details will be specified in the business cooperation agreement to be concluded by and between Taiwan Molly Digit Marketing Co., Ltd. and the Hong Kong company. Kunlun Beijing shall use its best efforts to assist the target group in establishing an entity for completing the operation of Target Business, transfer the license agreement signed by it with the local Copyright Society with respect to the copyrights to songs in Taiwan to this entity and assist this entity in concluding a cooperation agreement with the distributors in Taiwan and show host.



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- 5.10.2 Should the target group need to set up the framework of Variable Interest Entities (VIE) in China to operate the Target Business in the future, the Buyer shall cooperate with the target group and provide assistance in the establishment of the framework of Variable Interest Entities (VIE).
- 5.10.3 The Buyer and the Seller shall, since the establishment of WFOE, use all their reasonable endeavors to cause WFOE to complete the establishment of a branch ("Branch of WFOE") in Guangzhou, China within twenty (20) business days after the payment of the remaining consideration and cause the Branch of WFOE to pay the social insurance and housing fund for the employees specified in Part II of Annex 4. With respect to the employees specified in Part II of Annex 4, upon their execution of labor contracts with WFOE and prior to the establishment of Branch of WFOE, their social insurance and housing fund shall be paid by Beijing Foreign Enterprise Human Resources Service Co., Ltd. on behalf of WFOE, the expenses of which shall be borne by WFOE.

## **Article 6 Representation and Warranty**

### **6.1 Representation and warranty of each Warrantor**

Restricted by matters mentioned in disclosure letter (if applicable) in Annex 5, each Warrantor, collectively and jointly, makes representation, warranty and promise to the Buyer that, the Part I, Part III and Part IV in Annex 2 or warranty and disclosure matters, facts and information of other related Warrantors contained in this Agreement are unexceptionally real, correct and complete, and not misleading, during the period from signature day to the Closing date; and Part II, Part III and Part IV in Annex 2 or warranty and disclosure matters, facts and information of other related Warrantors contained in this Agreement are unexceptionally real, correct and complete, and not misleading, during the period from the Closing date to the Payment Date of the Remaining Consideration.

### **6.2 Representation and warranty of the Buyer**

The Buyer hereby makes representation and warranty to each Warrantor that, Part V in Annex 2 or warranty and disclosure matters, facts and information of other related Buyers contained in this Agreement are unexceptionally real, correct and complete, and not misleading, during the period from signature day to Payment Date of the Remaining Consideration.

## **Article 7 Other Promises**

### **7.1 Non-competition and non-solicitation**

- 7.1.1 The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea, collectively and jointly, make commitment to the Buyer that, since the Closing date, they will not (also to make sure that their affiliated parties (except each group company) and key persons will not) directly or indirectly, individually or collectively with other parties, or by establishing any other commercial entities directly or indirectly, individually or collectively with other parties engage in any businesses or activities (including research, development, marketing, promotion, provision of service and grant of permission) ("Restricted Business") that are same or similar with the target business or the target company or hold any rights and interests in such business or activities.





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- 7.1.2. The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea collectively and jointly, make commitment to the Buyer that, since the Closing date, they will not (also to make sure that their affiliated parties (except each group company) will not) in any form, whether directly or indirectly, hire any employees or former employees from any group companies, the Buyer or the Buyer's any affiliated parties, or solicit any employees or former employees from any group companies, the Buyer or the Buyer's any affiliated parties to engage in Restricted Business.
- 7.1.3. The Buyer makes a commitment to the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea that, in the event of transaction proposed by this Agreement being terminated pursuant to Clause 8.1.1 (b), the Buyer will not (also to make sure that its affiliated party will not) in any form, whether directly or indirectly, hire any Restricted Employees to engage in restricted business within the year since the date of termination. If (1) the Buyer or its affiliated party hires any Restricted Employees to engage in Restricted Business, and (2) the Buyer takes no necessary actions to correct within 5 business days since the Seller's notification on such employment in violation of the Buyer's commitment under this article, the Buyer should pay an indemnity of 10 million US dollars to the Seller within 10 business days upon receipt of the Seller's notification on such employment in violation of the Buyer's commitment under this article.
- 7.1.4. In case that any parts of this clause is deemed to be invalid, illegal or unenforceable in any aspects due to any reasons, such invalid, illegal or unenforceable parts shall not influence the effects of other parts of this clause, and this clause should be interpreted as such invalid, illegal or unenforceable parts never being contained in this clause. In this condition, the Clause 12.9 shall prevail. The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea agree that the Buyer may suffer the irreparable damage due to the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea's any violation to this article, and any indemnity for damage and relief is not enough to compensate the Buyer's damage due to such violation. The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea agree that the Buyer has the right to exercise injunctive relief to demand the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea's actual performance on this Clause 7.1. And the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea agree the exercise of such rights.
- 7.1.5. For the avoidance of doubt, any affiliated parties (except each group company) of the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea's violation of any regulations under this Clause 7.1 shall be deemed as acts of violation of the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea.
- 7.1.6. In the event that the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea are in violation of any regulations under this Clause 7.1, which shall be deemed as a serious breach of this Agreement, and the Buyer thus has the right to ask the breaching party for liquidated damages, with specific amount to be 2 million US dollars for each breach or the total amount of losses by the Buyer (subject to the higher one among them). The breaching party shall remit such amount into bank account designated by the Buyer as soon as possible, but under any circumstances which should never be later than ten (10) business days upon receipt by the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea of the Buyer's notification of requirement for such payment. Each party confirms and agrees that such amount is real estimation of loss possibly caused by related breaches, and is supplement of any other rights or relief that the Buyer can get pursuant to the law or the Contract, and under any circumstances any other rights or relief that the Buyer can get pursuant to the law or the Contract shall not be replaced or diminished.





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7.2 Incentive plan of management

7.2.1 The Seller agrees to transfer 15% ordinary shares of the Target Company it holds at Closing free of charge, so that the Target Company may hold them as Treasury Shares, and award them to the management in accordance with the incentive plan of management regulated in Shareholder Agreement and Articles of Association of the Target Company. For the avoidance of doubt, the Seller agrees that in case there are still outstanding Treasury Shares when incentive plan of management is terminated, this part of Treasury Shares shall not be returned to the Seller.

## Article 8 Termination

8.1 Termination of Agreement

8.1.1 This Agreement can be terminated and transactions proposed in this Agreement may be waived at any time under any of following circumstances:

- (a) with joint written consent of the Buyer and the Seller; or
- (b) if payment of the remaining consideration is not occurred before December 30, 2013, by the means of written notification by any breaching party of the Buyer or the Seller to send notification to the other party;

8.1.2 Besides, if any of the following circumstances happen before the Closing or the payment of the remaining consideration:

- (a) any Warrantors not punctually and effectively finish, follow or perform any obligations, promises or warranties it should finish, follow or perform under any transaction documents before the Closing date or the Payment Date of the Remaining Consideration, and such obligations, promises or warranties cannot be performed before the Closing date or the Payment Date of the Remaining Consideration after reasonable judgment;
- (b) representations or warranties under any transaction documents made by any Warrantors are unreal, incorrect, incomplete or misleading, or any such representations or warranties shall obviously become unreal, incorrect, incomplete or misleading, or occurrence of any incidents or circumstances causes or will cause representations or warranties under any transaction documents made by any Warrantors being unreal, incorrect, incomplete or misleading;
- (c) material adverse effects;
- (d) the Buyer does not punctually and effectively finish, follow or perform any obligations, promises or warranties it should finish, follow or perform under any transaction documents before the Closing date or the Payment Date of the Remaining Consideration, and such obligations, promises or warranties cannot be performed before the Closing date or the Payment Date of the Remaining Consideration after reasonable judgment;
- (e) Representation and warranty under any transaction documents made by the Buyer are unreal, incorrect, incomplete or misleading, or any such representation and warranty shall obviously become unreal, incorrect, incomplete or misleading, or occurrence of any incidents or circumstances cause or will cause representation and warranty under any transaction documents made by the Buyer being unreal, incorrect, incomplete or misleading;



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thus (i) under circumstances from (a) to (c), the Buyer has the right to make independent and careful decision, after having informed the Seller through written notification, to immediately terminate this Agreement and waive transactions proposed in this Agreement, and the Buyer does not have to bear any responsibility for such action. The buyer's right to terminate this Agreement pursuant to (a) to (c) above is additional and independent, and any exercises of such rights by the Buyer shall not influence and diminish any other rights, relief or claims which the Buyer shall get on the day of such notification, which shall also not constitute the waiver of such rights, relief and claims; (ii) under circumstances from (d) to (e), the Seller has the right to make independent and careful decision, after having informed the Buyer through written notification, of immediately terminating of this Agreement and waiving transactions proposed in this Agreement, and the Seller does not have to bear any responsibility for such action. The Seller's right to terminate this Agreement pursuant to (d) to (e) above is additional and independent, and any exercises of such rights by the Seller shall not influence and diminish any other rights, relief or claims which the Seller shall get on the day of such notification, which shall also not constitute the waiver of such rights, relief and claims.

## 8.2 Effectiveness of termination

- 8.2.1 Except situations regulated in Clause 8.3 below, this Agreement shall become invalid in case that this Agreement is terminated according to regulations of Clause 8.1 or regulations of applicable laws, but any responsibilities caused or incurred due to breach or any misrepresentations under this Agreement by each party shall not be exempted, and such termination shall not be deemed as waiver of any acquirable relief (including actual performance, if acquirable) upon any such breaches or misrepresentations.
- 8.2.2 If the termination incurs at any point-in-times ("Purchase-back Date") between the Closing date and the Payment Date of the Remaining Consideration, the Seller shall purchase back all shares of the Target Company held by the Buyer then, with purchase consideration of 1 USD or equivalent RMB (calculated according to central parity rate of USD against RMB published by the People's Bank of China on its official website on the fifth (5<sup>th</sup>) business day prior to Purchase-back Date).
- 8.2.3 If the termination incurs due to breaches of representations, warranties and promises under this Agreement or their obligation terms by each Warrantor, so that such transaction cannot be completed, thus they not only should return all funds in escrow account to the Buyer, but also need to compensate equivalent 10 million US dollars in the buyer's escrow account or equivalent amounts of RMB; if termination is due to breaches of representations, warranties and promises under this Agreement or their obligation terms by any buyers, so that such transaction cannot be completed, thus 10 million US dollars in the escrow account or equivalent amounts of RMB shall return to the Seller; but if termination incurs due to the remaining consideration payment's not being happened before December 30, 2013 and not due to breaches of representations, warranties and promises under this Agreement or their obligation terms by any parties, so that such transaction cannot be completed, thus all funds in the escrow account shall return to the Buyer, and all parties have no other indemnification obligations.

## 8.3 Continue to be effective

Regulations in this Clause 8, 9, 10, 11 and 12 continue to be effective after termination of this Agreement.



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## Article 9 Indemnity

### 9.1 Indemnity obligation of Warrantor

The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea hereby agree to, individually and jointly, compensate the Buyer, its affiliated party and their respective directors, management personnel, employees and (if permitted by applicable laws) agents, and protect them from all damages (including collateral and indirect damages), losses, debts, responsibilities, expenses and spending (including investigation costs and attorney fees as well as costs related with any actions, lawsuits or legal procedures) or impairment of value ("damages") (whether involved with claims proposed by the third party) which are associated with the following circumstances:

- 9.1.1 Any breaches of promises, representations and warranties made by each Warrantor under this Agreement;
- 9.1.2 Any types of appeals proposed by any person (including shareholders of the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea, the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea or any creditors of any affiliated parties of the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea) to question effectiveness of the whole or any parts transferred by Target Businesses and target assets or to impose or confirm restriction to the whole or any parts transferred by Target Businesses, target assets, Seller Shares or Shares to be Subscribed due to reasons which can be attributed to the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea;
- 9.1.3 Upon execution of any pledges or other encumbrances existing in Target Businesses or target assets on the Payment Date of the Remaining Consideration or prior to this date;
- 9.1.4 The Target Group does not follow any applicable laws on the Closing date or prior to the Payment Date of the Remaining Consideration, including any applicable laws and regulations on Target Business and target assets operation.
- 9.1.5 The Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea do not follow any applicable laws upon Target Businesses and target assets before Target Businesses and target assets being transferred to each group company according to reorganization plan;
- 9.1.6 Any reasons that can be attributed to each Warrantor leads to any transaction documents being completely or incompletely invalid, unenforceable or terminated;
- 9.1.7 The Seller does not perform related tax responsibility upon any transactions with Target Company or any transactions related with Target Company (including sale of the Seller Shares);
- 9.1.8 Responsibilities (including any debts, potential burden of taxation, potential social insurance and responsibility of housing funds payment or other responsibilities) related with Target Businesses and target assets which shall be borne by each Warrantor before any Target Businesses and target assets being transferred to each group company according to reorganization plan, such responsibilities shall be borne by target group because of transaction;
- 9.1.9 Claims caused by the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea by dismissing any employees related with Target Businesses before the Payment Date of the Remaining Consideration or within 90 days after the Payment Date of the Remaining Consideration, or caused by the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea's actions they have taken or not taken on any employees related with Target Businesses before the Closing date;
- 9.1.10 Any present or former owners of intellectual property do not properly pay award of inventor, remuneration of inventor, or any other awards or remunerations which legal requirement requires to pay to related inventor, designer or creator of such intellectual property prior to the Payment Date of the Remaining Consideration;



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- 9.1.11 In case that the Buyer is pursued by any domestic or overseas tax authorities for tax which shall be borne by each Warrantor at any time-points after the Payment Date of the Remaining Consideration; and
- 9.1.12 Any types of appeals existing upon any facts or situations and used by target group over ownership of any intellectual properties that were produced before the Payment Date of the Remaining Consideration, including: (1) any queries upon exclusive and limitless ownership over intellectual property, or any propositions of rights, interests or benefits of any nature existing in it, or (2) being charged of violating intellectual property of any third party.
- 9.2 Buyer's obligation of indemnification
- The Buyer hereby agrees to indemnify the Seller, Seller's directors, managers, employees and agents (under the permission of applicable laws) against all damages individually and jointly (whether concerning third party's claims or not) in the case of the following circumstances:
- 9.2.1 Any violation of Buyer's commitment, representation and warranty provided in the Agreement;
- 9.2.2 If any transaction document becomes invalid, unenforceable or terminated in whole or in part due to the Buyer.
- 9.3 Other remedies
- The Parties recognize and agree that the indemnity articles provided in Article 9 hereof are in addition to, and do not exclude any other rights and remedies provided by law or equity.

#### Article 10 Confidentiality

- 10.1 Confidentiality Obligation
- Each Party hereof shall strictly keep the information contained herein or acquired or obtained due to the negotiation and/or execution hereof in confidence and shall not disclose or use such information, including any information related to the following items:
- 10.1.1 The existence of the Agreement and the provisions hereof;
- 10.1.2 Negotiation related to the Agreement; or
- 10.1.3 Business activity of any Party hereof, of such Party or of any of their affiliates.
- 10.2 Permitted Disclosure
- Provided, however, that in the following cases, Article 10.1 shall not be applied to the disclosure or use of any information to the following extent:
- 10.2.1 Disclosure or use required by applicable laws, by any rules of the stock exchange where share of any Party listed in or by any governmental authority, provided that related Party shall inform other parties about such requirement prior to the disclosure or the use to provide other parties with an opportunity to refuse such disclosure or use or to discuss the time and content thereof;
- 10.2.2 Disclosure or use necessary for the purpose of any legal procedure arising from the Agreement or from any other agreements executed hereunder or pursuant hereto, or the disclosure is made to any tax authority due to tax affairs related to the disclosing party;
- 10.2.3 Disclosure made to the managers, directors, employees, lawyers, accountants, financial consultants and other agents or representatives (hereinafter referred to as "Representatives") of any Party who requires learning such information for the purpose of completing transactions hereunder or under other agreements concluded pursuant hereto, provided that such representative undertakes to comply with Article 10.1 in respect of such information, as if it is a party hereof;



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- 10.2.4 Such information may be acquired from public domain [except such information may be acquired as a result of breaching the Confidentiality Agreement (if any) or the Agreement]; or
- 10.2.5 Written consents have been made by other parties prior to the disclosure or use.

#### **Article 11 Public Statement**

The Parties agree to negotiate with other Party in case of making any news release or public statement regarding the Agreement or any transactions described in the Agreement. No news release or public statement shall be made before negotiation except where required by applicable laws or listing rules of any securities exchange upon which shares in any Party are listed. Notwithstanding the provisions of this Article 11, the Buyer shall make an announcement regarding each group company or its own operation, business or asset without prior negotiation with the Seller after the payment date of the remaining consideration.

#### **Article 12 General Provisions**

- 12.1 Each Party's responsibility for tax liability, cost and expense
  - 12.1.1 Each Party shall bear its own respective tax liability arising out of the performance of the transaction in accordance with the applicable laws and any consequences in connection with the above tax liability.
  - 12.1.2 Each Party shall bear its own fees (whether paid or to be paid) in respect of due investigation concerning transaction and any fees arising out of the preparation, negotiation of transaction documents and other relevant documents, including the fees paid to lawyers, accountants and other professional advisors, negotiation and preparation fees related to the Agreement and other transaction documents as well as the fees arising out of the performance of transaction.
- 12.2 Binding; Transfer
 

The Agreement shall be binding upon all Parties, their respective successors and permitted transferee and shall be enforceable. No Party may transfer any of their rights or obligations hereunder without the prior written approval of other parties, provided that the Buyer shall have the right to transfer its rights in whole or in part hereunder to its any Affiliates without Seller's prior written consent.
- 12.3 Governing Law
 

The Agreement shall be governed by and construed in accordance with the laws of Hong Kong.
- 12.4 Dispute Settlement
  - 12.4.1 Any disputes, controversies or claims (respectively as a "Dispute") arising out of or relating to the Agreement or the interpretation, violation, termination or validity of the Agreement shall be resolved on the basis of mutual negotiation. The negotiation shall be started upon the delivery of a written notice by any party to any other parties requiring so.
  - 12.4.2 In the event that such Dispute fails to be resolved within sixty (60) days after the delivery of such notice, such Dispute shall be submitted for arbitration upon the delivery of a written notice (hereinafter referred to as "Arbitration Notice") by any disputing party to any other parties requiring so.



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- 12.4.3 The Dispute shall be submitted to the Hong Kong International Arbitration Centre (“HKIAC”) and be arbitrated in Hong Kong. The arbitration shall be made by three (3) arbitrators who shall be appointed pursuant to the arbitration rules of HKIAC (“Arbitration Rules”) in effect at the arbitration unless otherwise expressly provided in Article 12.4.3. The Buyer shall nominate one arbitrator; if the Sellers are involved in relevant arbitration, the Seller shall jointly nominate one arbitrator within ten (10) days after the Buyer’s nomination of an arbitrator, in the case of failure of such nomination, the arbitrator shall be nominated by HKIAC; the third arbitrator shall be the chief arbitrator who is nominated by each Party’s arbitrator jointly after the nomination of arbitrator on later date; if such nomination fails, the chief arbitrator shall be nominated by HKIAC.
- 12.4.4 The arbitration proceedings shall be conducted in Chinese. The arbitration court shall apply the Arbitration Rules.
- 12.4.5 The arbitration award made by the arbitration court shall be final and binding upon the Parties; the winning party may apply the execution of such award with the court with jurisdiction.
- 12.4.6 Any party involved in the Dispute shall be entitled to seek temporary injunctive relief in any court with jurisdiction, where practicable.
- 12.4.7 The Agreement shall be continuously performed during the arbitration course except the part to be arbitrated.
- 12.4.8 The arbitration fee shall be undertaken by the losing party in the arbitration pursuant to the arbitration award, including legal fee, accountant fee and costs and expenses for other professionals arising from the survey, collection, prosecution and/or defense made by any winning party for any request in dispute.
- 12.5 Amendment
- Unless otherwise permitted herein, any amendment, change, waiver, cancellation or termination hereof or of any provisions herein shall be made in written documents signed by each Party.
- 12.6 Notice
- 12.6.1 All notices, claims for rights, certifications, requests, requirements and other communications given to any other Party hereunder shall be made in writing and shall be delivered to such party by person, facsimile or overnight courier service of good faith with a prepaid postage at the address listed in Article 12.6.2 or at any other addresses pointed by such party in a notice to other parties. Such communications shall be deemed as delivered (i) at its delivery if by hand; (ii) upon receiving the receipt if by facsimile; and (iii) within five (5) calendar days after being delivered to or received by the courier.
- 12.6.2 The notices hereunder shall be delivered to the Parties at following addresses and received by the following person:
- Seller: Koram Games Limited.
- Address: Suite 5118, 51th Floor, Hopewell Centre, No. 183 Queen’s Road East, Wanchai, Hong Kong
- Fax: 00852-36023071
- Attn.: Zhou Yahui



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Buyer: HEROIC VISION HOLDINGS LIMITED

Address: Floor 2, East Tower, Jingyan Building, No. 29 Shijingshan Road, Shijingshan District, Beijing

Fax: 86-10-68874008

Attn.: Legal Department of Heroic Vision

Kunlun Beijing: Beijing Kunlun Technology Co., Ltd.

Address: Tower B, Mingyang International Center, No. 46, Xizongbu Alley, Dongcheng District, Beijing

Fax: 86-10-65210297

Attn.: Zhou Yahui

Kunlun Guangzhou: Guangzhou Kunlun Online Information Technology Co., Ltd.

Address Third Floor, No. 44 Jianzhong Road, Tianhe Software Park, Tianhe District, Guangzhou

Fax: 020-85665608-8008

Attn.: Zhou Yahui

Kunlun Korea: Kunlun Korea Co., LTD

Address: 10F823Bldg, 823-16 Yeoksam-Dong, Gang-nam Gu, Seoul, Korea

Fax: 82-02-568-6260

Attn.: Zhou Yahui

12.7 Further Warranty

Each Party shall make and perform (or cause other party to make and perform) all further actions and matters and shall execute and deliver all other agreements, certificates, instruments and documents, which may be reasonably required by any other parties for the achievement of the provisions and the purpose hereof.

12.8 Entire Agreement

The Agreement and all other transaction documents shall jointly constitute the entire agreement among the Parties in respect of the subject hereof and supersede all previous written or oral understandings or agreements.

12.9 Severability

If any provisions hereof are deemed as void or unenforceable to some extent, the remaining provisions shall not be affected and shall be performed to the maximum extent permitted by law. Any invalid or unenforceable provisions of the Agreement shall be replaced by other valid and enforceable provisions, and such provisions shall have the proximal effectiveness with the original meaning of unenforceable provisions herein.

12.10 Cumulative Remedies

All rights and remedies provided for herein or obtained in other ways shall be accumulated and exercised in succession with all other rights and remedies.

12.11 Counterparts

The Agreement may be executed in one copy or any number of counterparts, each of which shall be deemed as an original but all of which shall constitute one and the same instrument.





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**IN WITNESS WHEREOF**, the Parties hereto have executed the Agreement as of the day and year first above written by duly authorized representatives of each Party and the Parties hereto duly established in China shall affix their official seals.

Koram Games Limited

Signature: /s/ Zhou Yahui

Name: Zhou Yahui

HEROIC VISION HOLDINGS LIMITED

Signature: /s/ Wang Tao

Name: Wang Tao

Beijing Kunlun Technology Co., Ltd. (seal)

Signature: /s/ Zhou Yahui

Name: Zhou Yahui

Guangzhou Kunlun Online Information Technology Co., Ltd. (seal)

Signature: /s/ Zhou Yahui

Name: Zhou Yahui



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Kunlun Korea Co., LTD

Signature: /s/ Zhou Yahui

Name: Zhou Yahui



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Annex I Definition	
“Confidentiality and Non-competition Agreement”	It refers to the Confidentiality and Non-competition Agreement signed between the Target Company and each target business employee, whose content and form shall satisfy the Buyer and the Seller.
“Warrantor’s Warranty”	It refers to the representation and warranty included from Part I to Part III of Annex II.
“The Agreement”	It has the meaning stipulated in the preface hereof.
“Encumbrance”	It refers to mortgage, charge (fixed or floating), inhibition, balancing method, guaranty, pledge (legal or not), right of the first refusal, share option, claim, ownership retained, priority right, security interest or rights of the third parties or any kinds of encumbrance on other properties or rights of any nature or by itself.
“Reorganization Plan”	It refers to the reorganization plan of the Target Group included in Annex III.
“Representative”	It has the meaning stipulated in Article 10.2.
“Shares to Be Subscribed”	It has the meaning specified in Article (3) of the Agreement.
“Each Warrantor”	It has the meaning stipulated in the preface hereof.
“Parties” or “Party”	It has the meaning stipulated in the preface hereof.
“Group Company”	It refers to the Target Company (after it is established), Hong Kong Company (after it is established) and WFOE (after it is established) which are hereinafter referred to as the “Target Group” collectively and “Group Company” respectively.
“Shareholder Agreement”	It refers to the Shareholder Agreement regarding the Target Company, signed among the Buyer, the Seller and the Target Company with consistent content and Appendix I.
“Key Person”	It refers to Xiang Gensheng, Hu Bin, He Renxiu, Lin Duanqun, Wu Xulan and Shen Lifeng.
“Related Party”	As for any subject, (i) if it is a natural person, it refers to the spouse and direct relative of this person (no matter it is consanguinity or adoption relation between them) and the trust established and existed for the benefit of this person or its spouse, parents or children; (ii) if it is a legal person, unincorporated organization and institution and the entity with other form, It refers to any party to control this subject directly or through one or multiple intermediaries, any party controlled by the subject directly or through one or multiple intermediaries or any party with the subject controlled by a party directly or indirectly. “Control” refers that (i) a party owns over 50% voting stock, registered capital or other equity capital of the other party directly or indirectly, no matter through owning security and by contract or other methods; or (ii) owns the right to appoint the management, board of directors or most members of similar decision-making body.



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<b>“HKIAC”</b>	It has the meaning stipulated in Article 12.4.3.
<b>“Korea”</b>	It refers to the Republic of Korea.
<b>“Closing”</b>	It refers that the Buyer or the Seller has exempted the condition correspondingly that the prerequisites of Articles 3.1 and 3.2 have been satisfied or not been satisfied and all the shares and the shares to be transferred of the Seller are transferred and issued to the Buyer appropriately.
<b>“Closing Date”</b>	It has the meaning stipulated in Article 5.1.
<b>“Transaction”</b>	It refers to the transaction implemented in accordance with the Agreement.
<b>“Transaction Document”</b>	It refers to the documents related to transaction, including the Agreement, Shareholder Agreement, Labor Contract, Confidentiality and Non-competition Agreement, Business Cooperation Contract and other documents that will be concluded in accordance with above documents or those ones related thereto.
<b>“Kunlun Beijing”</b>	It has the meaning stipulated in the preface hereof.
<b>“Kunlun Guangzhou”</b>	It has the meaning stipulated in the preface hereof.
<b>“Kunlun Korea”</b>	It has the meaning stipulated in the preface hereof.
<b>“Labor Contract”</b>	It refers to the Labor Contract signed between the Target Company and every target business employee, whose content and form shall satisfy the Buyer and the Seller.
<b>“The Buyer”</b>	It has the meaning stipulated in the preface hereof.
<b>“Buyer’s Warranty”</b>	It refers to the representation and warranty included in Part V of Annex II.
<b>“The Seller”</b>	It has the meaning stipulated in the preface hereof.
<b>“Seller’s Shares”</b>	It has the meaning in Article (3) hereof.
<b>“US Generally Accepted Accounting Principles”</b>	It refers to the US Financial Accounting Standards, methods and procedures specified by the US Financial Accounting Standard Board, Institute of Accountants and Securities and Exchange Commission.



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<b>“Daily Active Users (DAU)”</b>	It refers to the users who successfully log in the RC voice service (www. raidcall. com), contribute their integrals and stay on line for at least one minute on the date of statistic, excluding the users log in repeatedly.
<b>“Dollar”</b>	It refers to the legal currency of the United States of America.
<b>“Financial Data”</b>	It refers to the financial data of operating result and asset balance condition issued before the Closing Date, reviewed through accounting firm as of September 30, 2013 and made regarding target business and target asset.
<b>“Target Company”</b>	It has the meaning stipulated in Article (2) hereof.
<b>“Articles of Association of the Target Company”</b>	It has the meaning stipulated in Article 3.1.14.
<b>“Target Group”</b>	It refers to the Target Company (after it is established), Hong Kong Company (after it is established) and WFOE (after it is established) which are hereinafter collectively referred to as the “Target Group” and the “Group Company” separately.
<b>“Target Business”</b>	It has the meaning stipulated in Article (1).
<b>“Target Business Employee”</b>	It refers to the person listed in Article 1.2 of Part I, Article 1.2 of Part II and Article 1.2 of Part IV of Annex IV.
<b>“Target Asset”</b>	It has the meaning stipulated in Article (1) hereof.
<b>“Ordinary Shares”</b>	It refers to the ordinary shares of the Target Company, whose par value is USD 1.00 per share. Its right and obligation are specified in the Articles of Association of the Target Company.
<b>“Signing Date”</b>	It refers to the date first written in the Agreement.
<b>“RMB”</b>	It refers to RMB, the legal currency of China.
<b>“Payment of the Remaining Consideration”</b>	It refers that the Buyer or the Seller has exempted the condition that the prerequisites of Article 3.3 have been satisfied or not been satisfied. The Buyer pays the remaining transfer consideration and the remaining subscription consideration and transfers the initial transfer consideration in the escrow account into the Seller’s account.
<b>“Payment Date of the Remaining Consideration”</b>	It has the meaning stipulated in Article 5.5.
<b>“The Remaining Subscription Consideration”</b>	It has the meaning stipulated in Article 2.3.2.
<b>“The Remaining Transfer Consideration”</b>	It has the meaning stipulated in Article 2.3.1.



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**“Business Cooperation Agreement”**

It refers to the Business Cooperation Agreement whose content and form shall satisfy the Buyer and the Seller reasonably, regarding carrying out target business continuously for Taiwan Molly Digit Marketing Co., Ltd..

**“Applicable Law”**

It refers that regarding any person, on or after, the Signing Date hereof and every revision, it can be applicable effectively to any constitution, treaty, statute law, law, rule, regulation, criterion, ordinance, judgment, order, decree, adjudication, prohibition, government permission, examine and approval, award, permission, agreement, command, request or limitation or any decision made by any government department with similar form, or identification made by it, or any explanation of above any content or any or all enforced regulations of this person, its subsidiary or corresponding asset.

**“Initial Transfer Consideration”**

It has the meaning stipulated in Article 2.3.1.

**“Tax”**

It refers to the related tax of income, sale and use, enforcement, special permission, immovable property and estate, total revenue, capital stock, production, business and profession, transfer, register, profit, resource, permission, document, disability, employment, salary, severance pay and withholding or other kinds of tax, expropriation, apportion, tariff or charge imposed by any government department, any tax related interest and penalty, unpaid or unpaid enough (civil or penal), and any loss or tax responsibility of related adjudication, reconciliation and lawsuit of any responsibility produced from it.

**“Damage”**

It has the meaning stipulated in Article 9.1.

**“Escrow Account”**

It refers to the offshore bank account opened jointly by the Buyer and the Seller and managed by the escrow agent. The Buyer and the Seller will sign escrow agreement with the agent.

**“WFOE”**

It has the meaning stipulated in Annex III “Reorganization Plan”.

**“WFOE Branch Office”**

It has the meaning stipulated in Article 5.10.3.

**“Foreign Exchange Department”**

It refers to the State Administration of Foreign Exchange and/or other corresponding local branches (as appropriate).

**“Restricted Business”**

It has the meaning stipulated in Article 7.1.1.



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<b>“Restricted Employee”</b>	It refers to the target business employee and the following persons: * (ID Number: *) * (ID Number: *) * (ID Number: *) * (ID Number: *) * (ID Number: *) * (ID Number: *)
<b>“Hong Kong”</b>	It refers to Hong Kong Special Administrative Region.
<b>“Hong Kong Company”</b>	It has the meaning stipulated in Annex III “Reorganization Plan”.
<b>“Permission”</b>	It refers to any approval, permission, exemption, acceptance, filing, register, notification or other authorization.
<b>“Accounts Payable”</b>	It has the meaning stipulated in Annex III “Reorganization Plan”.
<b>“Business Day”</b>	It refers to any calendar day except Saturday, Sunday or legal holidays of China, British Virgin Islands and Hong Kong, China.
<b>“Dispute”</b>	It has the meaning stipulated in Article 12.4.1.
<b>“Security”</b>	Regarding one company, it refers to (i) its stock rights, share or voting security; (ii) the security that can be transferred or replaced into stock rights or voting security; and (iii) the share option, warrant, or other rights (including transformation right or pre-emption right and preemption right), any stock rights, share or voting security purchased from it or issued obligatorily by it and the security that can be transferred or replaced into stock right or voting security.
<b>“Intellectual Property”</b>	It refers to the intellectual property listed in Annex VI hereto.
<b>“China”</b>	It refers to the People’s Republic of China, excluding Hong Kong Special Administrative Region, Macao Special Administrative Region and Taiwan only for the purpose hereof.
<b>“Chinese Accounting Standard”</b>	It refers to the Ministry of Finance of the People’s Republic of China, Chinese Institute of Certified Public Accountants and all accounting systems, principles, standards and guidelines issued or revised from time to time by related organization of power.
<b>“Industrial and Commercial Administration of China”</b>	It refers to the State Administration for Industry & Commerce and/or other corresponding local branches (as appropriate).

**The symbol “\*” in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.**





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<b>“Commercial Department of China”</b>	It refers to the Ministry of Commerce and/or other corresponding local branches (as appropriate).
<b>“Arbitration Rules”</b>	It has the meaning stipulated in Article 12.4.3.
<b>“Arbitration Notice”</b>	It has the meaning stipulated in Article 12.4.2.
<b>“Material Adverse Effect”</b>	It refers to any event, issue, situation, change or development which results or may result into material adverse effect within rational expectation. Regarding the following situations specifically: (i) for the Buyer, if breach, situation, change, influence or other situations result that the Buyer cannot perform its obligation hereunder or result that it cannot complete the expected transaction herein; (ii) for each the Warrantor, if such breach, situation, change, influence or other situations result that the Warrantor cannot perform its obligation hereunder (including the steps of carrying out the Reorganization Plan) or result that it cannot complete the expected transaction herein; or (iii) for the Target Company, if breach, situation, change, influence or other situations separate or accumulate to result that daily active users (“DAU”) reduce 20% or more for the target business in the non-Chinese land or result the demission of any key person in the Target Company.
<b>“Transfer Consideration”</b>	It has the meaning stipulated in Article 2.3.1.



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## **Annex II Representations and Warranties**

### **Part I Closing Warranty**

#### **1. Equity Capital**

1.1 The equity capital authorized by the Target Company shall be USD 50,000, and the issued equity capital shall be USD 7,500, which is 7,500 ordinary shares with a par value of USD 1.00 per share and has been paid fully.

1.2 After the transaction, the Buyer shall legally, effectively, completely and exclusively own the equity of the Target Company but have no encumbrance and no obligation to further invest in the Target Company under any law or the Contract. Except the equity capital issued, the Target Company shall have no outstanding stocks.

#### **2. Information on the Target Company**

2.1 The information on the Target Company listed in Annex II shall be authentic, complete and accurate.

2.2 The Memorandum and Articles of Association of the Target Company submitted to the Buyer shall be authentic, complete and accurate according to the requirement of the applicable laws. The Target Company shall violate no clause or provision stipulated in these documents.

2.3 The Target Company's shareholder list and other statutory books shall be legally prepared and kept properly, have reflected the latest situation, and have accurately and completely recorded all the matters these books shall deal with. The minute books for the board meeting and the shareholders' meeting shall have accurately recorded all the resolutions passed by the Target Company's directors and shareholders separately. All the records, announcements, registrations and other procedures the applicable laws require the Target Company to deliver or make shall have been delivered or made on time.

2.4 The Target Company shall have no subsidiaries, branches, joint ventures or other investments.

2.5 Unless otherwise authorized by the board of directors, the Target Company shall have not made any authorization that is still effective on the Signing Date and the Closing Date, and anyone (no matter the agent or other person) shall have no right to restrict or procure the Target Company to bear any obligation.

#### **3. Compliance with Laws**

3.1 The Target Company shall not violate, and have not violated any applicable laws, including the national laws, regulations and local rules issued by the judicial areas where it operates businesses and applicable to the Target Company or its businesses.

3.2 The completion of the transaction proposed hereunder shall not (i) lead to a violation of any document of the Target Company; (ii) lead to a conflict with any applicable law; (iii) lead to a violation by the Target Company of any clause stipulated in any contract, or lead to the termination, rescission or advance of the Target Company's rights and obligations under any clause stipulated in any contract, or lead to loss of the Target Company's any interests under any clause stipulated in any contract, or lead to any enhancement in the Target Company's existing effective interest rate for its debts; (iv) lead to any encumbrance of the Target Company's any property or asset; or (v) lead the Target Company to be unable to or difficult to own and operate its businesses in its intended ways.



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- 3.3 All the contracts with the Target Company as one of the contracting parties shall be effective and binding on the contracting parties, meanwhile the Target Company along with its opposite parties to the above contracts shall abide by the clauses hereof in terms of all important aspects. The Target Company shall have not received any notice on termination of these contracts or intention to terminate these contracts.
- 3.4 The following events have not occurred, and the following situations (no matter whether the notice is required or not or the time lapses) do not exist: (i) events or situations that may lead the Target Company to violate or not to abide by any applicable law; or (ii) events or situations that may lead the Target Company to have an obligation to take any remedial action or bear all or part of costs for such remedial actions. The Target Company shall have not received any notice or other communications (either in oral or in written form) from any government department on (x) any actual, alleged, possible or potential violation or noncompliance of any applicable laws, or (y) the Target Company's obligation to take any actual, alleged, possible or potential remedial action or bear all or part of the costs for these remedial actions.
4. No Appeal or Lawsuit
- 4.1 No appeal shall be pending or threatened to be proposed for the Target Company or its businesses, or doubt, or seek for preventing, prohibiting, changing or delaying the transaction proposed in the Agreement in any way. The Target Company or its businesses shall not have involved in or be expected to involve in an appeal in any way which can exert partially or entirely significant adverse impact. No facts or situations that may lead to an investigation and disciplinary measure for the appeal shall exist.
- 4.2 No unredeemed judgment, court order, tribunal or arbitration award for the Target Company or its businesses shall exist, and no detention, implementation or procedure on the above matters shall exist.
- 4.3 Any person who may bear the responsibility for its action or error due to the Target Company or its businesses shall not be involved in any appeal as a plaintiff, defendant or other identity. No facts or situations that may lead to an investigation and disciplinary measure for the appeal shall exist.
- 4.4 No unredeemed judgment, court order, tribunal or arbitration award for any person who may bear the responsibility for its action or error due to the Target Company or its businesses shall exist, and no partial detention, implementation or procedure on the person or its assets shall exist.

#### 5. Prevention of Bribery Ordinance

The Target Company or any of its representatives shall not directly or indirectly provide, pay, promise to pay or authorize to pay any money, or provide, promise to give or authorize to give any valuable objects to any government officer or any political party (or any person, when the Target Company or any of its representatives knows or realizes that, all or part of such money or valuable objects are probable to be directly or indirectly provided, given or promised to be given to any government officer or any political party) or personnel or officer of private enterprise, state-owned enterprise or investment companies, or their relatives or other specified person for the following purposes:

- 5.1 (x) Influence the government officer or political party's any action or decision made as the officer identity, (y) induce the government officer or political party to violate its legal responsibility to make or not make any action, or (z) obtain any improper advantage;



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- 5.2 Influence or induce the authorization of any contract to the Target Company or its related party, or obtain any other advantage for the Target Company or its related party in other ways, or retain the Contract after one contract has been authorized to the Target Company or its related party;
- 5.3 Directly or indirectly assign the payment for or interests obtained from any person's sales or purchases (or agreeing to sales or purchases) of goods or services to a government officer or any of its relatives or specified person; or
- 5.4 Undertake any matter that may violate, seemingly violate or lead the Target Company or its related parties to violate any applicable law.
6. Bankruptcy
- 6.1 The Target Company shall not be bankrupt or be unable to pay due debts under applicable law.
- 6.2 There shall be no procedure related to any compromise or arrangement with the creditors; no closure, bankruptcy or other dissolution process related to the Target Company or its businesses; there shall be no events that shall trigger these procedures under the applicable law.
- 6.3 The Target Company or its businesses shall not be subject to the control by any insolvency administrator or recipient.
7. Financial Records
- 7.1 The Target Company shall properly make and retain all account books, register and records in accordance with applicable laws.
- 7.2 All accounts, account books, ledgers, financial records, and other records retained by the Target Company in accordance with applicable laws, rules and regulations:
- (a) Shall be held by the Target Company or its duly authorized agent;
  - (b) Shall be properly retained and reflected the recent condition;
  - (c) Shall be free of any type of error and deviation (except for unintentional slight or unsubstantial error); and
  - (d) Fairly reflect the truth of all financial transactions and financial affairs, contracts and trading condition of the Target Company.
8. Events Occurring After the Establishment of the Target Company
- 8.1 Since the establishment of the Target Company, except for being required by regular services or business deals of the Target Company:
- (a) Business of the Target Company shall be conducted and/or expanded in accordance with regular services operations and/or the actual situation in order to maintain the continued viability of its business and not to change the managements or operations of its business, undertaking or assets, except for changes in consistent with inherent practice or business expanding in accordance with actual situations;
  - (b) There shall not be any event that will have any significantly adverse effects on assets and liabilities, financial position, trading conditions, and prospects of the Target Company;
  - (c) No modification of the Target Company's organizational documents shall occur (whether through merger, combination or other forms);
  - (d) No change in the directors of the Target Company;



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- (e) The Target Company shall not acquire, directly or indirectly, any assets, stocks, property, interests or business (whether through merger, combination, stock rights or asset acquisition, or other forms), except for the supply in consistent with the previous business operation within the scope of regular service (if applicable);
- (f) The Target Company shall not issue, deliver or sell any share of any securities, or authorize to issue, deliver or sell the same (whether by merger, combination, initial public offering or other forms);
- (g) No dissolution, bankruptcy, cancellation, liquidation or reorganization shall occur in the Target Company;
- (h) The Target Company shall not split, combine, or reclassify any stocks, or announce, withdraw or pay any dividend or other distribution in respect of stocks (whether in cash, stock, property or other combinations), or redeem, repurchase or otherwise acquire any stocks, or offer to redeem, repurchase or otherwise acquire any stocks;
- (i) Unless required by applicable laws, the Target Company shall not (i) establish, adopt or amend any collective negotiation, awards, profit sharing, savings, pension, retirement, deferred compensation, recompense, stock options, restricted stock or other benefit programs or arrangements of its directors, officers or employees; or (ii) add any recompense, rewards or other payable benefits, severance pay or termination fees for its director, officer or employees (or amend any existing arrangements);
- (j) The Target Company shall not make any capital expenditure or any capital commitments that are more than RMB 300,000 beyond the scope of regular service;
- (k) The Target Company shall not set, have, assume or receive any borrowings of debt or warranty, and shall not be bound by or be required to pay back in advance any outstanding borrowings by the Signing Date and Closing Date of the Agreement;
- (l) The Target Company shall not: (i) acquire any asset of any nature with the amount more than RMB 300,000; (ii) sell, transfer or otherwise dispose in other forms any assets of any nature with the amount more than RMB 300,000; or (iii) fully or partially cancel or waive or terminate or sell at a discount any debt or request of right;
- (m) The Target Company shall not: (i) compromise, offer or propose compromise; (ii) apply to litigation, investigation, arbitration, procedure, or other request of rights; (iii) apply to any shareholder litigation or dispute against any of its officers or directors; or (iv) apply to any litigation, arbitration, procedure or dispute relating to the Agreement;
- (n) The Target Company shall not appoint or change the auditors, change tax choice, confirm or change tax accounting year period, adopt or alter tax accounting methods, modify tax declaration or submit tax refund requests, reach tax compromise agreement, settle tax claims, audit or collection, or give up claims on refund of duty, tax offset or other cuts on tax liability;
- (o) The Target Company shall not sell, lease, or otherwise transfer any assets, stocks, property, interests or business, or set or generate any encumbrances on them;
- (p) The Target Company shall not provide any loan, advance payment (except for advance payments that are in consistent with the previous operation) or capital contributions to any other person, or investments for, or assurances, compensation, joint liability or other warranty made by or for the benefit of the other person; and
- (q) The Target Company shall not violate any debt, mortgages, contracts, or any rules or regulations of any applicable laws.



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8.2 Compliance with the terms of the Agreement will not:

- (a) Be in contradiction with any terms, rules and regulations of any agreement or document signed by the Target Company as a party (the Agreement or document is still in force and/or uncompleted on the Signing Date and Closing Date of the Agreement), or any rules of any memorandum and Articles of Associations of the Target Company, or any encumbrances, leases, contracts, commands, judgment, adjudication, prohibitions, rules, or other restrictions of any type or nature that have binding force or jurisdiction on any Target Company or its assets on the Signing Date and Closing Date of the Agreement; or in contradiction with obligations, or lead to the violation of or violate any forgoing items;
- (b) Relieve any obligation (whether contractual obligations or other obligations) of any person to any Target Company;
- (c) Cause any assets of any Target Company to be set, forced to set any encumbrance or make such encumbrances specific or enforceable; or
- (d) Cause any current or future debt of any Target Company to expire or be declared as due and payable before the specified expiration date.

8.3 The Target Company shall not agree to become a member of any joint venture, associated enterprise, partnership or other non-group company; the Target Company is not and did not agree to become a party to any commission or other revenue-sharing agreement or arrangement.

9. Assets

9.1 All of the assets purchased by the Target Company and having not been disposed in regular services belong to the Target Company. The assets shall not be attached with any encumbrances or any installment arrangement.

9.2 Since the establishment day of the Target Company, the assets shall be held and managed by the Target Company, and be continuously available (subject to normal loss), within reasonable request and meeting its design or purchase purposes in its regular services.

9.3 On the actual knowledge of each Warrantor or what shall be reasonably known after proper inquiry or doing duty of care, there shall not be any factor that would cause difficulties to recover accounts receivable and other amounts due that are generated within the scope of the regular services of the Target Company by the Closing Date, and the foregoing amounts shall not have any dispute or counterclaim and shall not be offset.

10. Real Estate

10.1 The Target Company shall not be entitled to any legal property and property of beneficial interests or other rights or interests of any real estate.

10.2 Each lease constitutes an entire agreement of its real estate concluded by the Target Company as a party. Each true and complete copy of the lease, together with all modifications, changes, alterations that have been made thereto, shall be sent to the Buyer. Each lease shall be validly existing and enforceable to the Parties in accordance with its terms. Each lease shall be registered and recorded. On the Signing Date, all precedent conditions for each lease to be enforceable shall all be met. The Target Company shall accept and actually possess the real estate in accordance with the respective lease, and shall not be subleased, released, or pledged its leasehold interest.



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- 10.3 Target Companies shall always promptly pay any rent or other payable fees and costs in accordance with the leases. In the terms of any lease, there shall not be any default or event of default of the Target Company that have not yet been remedied or waived, or the default or event of default that occurred when the notification was issued, by the elapse of time or both. There shall not be any pending or eventual expropriation, confiscation, disputes, claims, demands, or similar procedures relating to or may affect the continued use and enjoyment of any lease.
- 10.4 Landlord of each lease shall have full property rights of the real estate under the lease without any property defects. Each real estate under any lease shall be in all respects consistent with applicable laws and appropriate for the Target Company's business operations. Each lease and the Target Company shall be continuously used, occupied, and operated in the way used, occupied and operated currently. The real estate under the lease shall not constitute any violation relating to architecture, planning, fire control, partition and other land use and similar applicable laws.
11. Material Contracts
- 11.1 In addition to the provisions of the Agreement, any agreement, document or arrangement concluded by the Target Company as a party shall be free of any relevant non-performance, breach of contract negligence that may lead to any request of right that exists by the Signing Date of the Agreement and will have significantly adverse effect to the Target Company. There shall not be any possibility for the request of right to occur or any circumstances which may trigger the request of right.
- 11.2 On the actual knowledge of each Warrantor or what shall be reasonably known after proper inquiry or doing duty of care, all Parties that conclude the Agreement with the Target Company or incur obligation to the Target Company shall not violate the Agreement with the Target Company or the obligations to the Target Company. The Target Company shall not violate any agreement or agreements it concludes as a party (such agreement or agreements are still in force and/or uncompleted on the Signing Date and Closing Date of the Agreement) to cause significant adverse effect on the Target Company.
- 11.3 On the actual knowledge of each Warrantor or what shall be reasonably known after proper inquiry or doing duty of care, there shall not be any offer, bid, or similar matter that has significant adverse effect on overall business or financial position of the Target Company.
- 11.4 The Target Company shall not conclude or assume any contract, transaction, arrangement or obligation that meets the following conditions (such contract, transaction, arrangement or obligation is still in force and/or uncompleted on the Closing Date, and the amount of money involved is more than RMB 300,000, except for those obligations of the Target Company under these contracts, transactions, arrangements or obligations that have already been disclosed accurately in the disclosure letter): special or unusual nature, or beyond the scope of the regular service.
- 11.5 On the actual knowledge of each Warrantor or what shall be reasonably known after proper inquiry or doing duty of care, any of the group companies shall not be subject to any default remedial responsibility or obligation.
- 11.6 On the Signing Date, the Agreement, all contracts or arrangements concluded by the Target Company (such contract or arrangement is still in force and/or incomplete on the Closing Date) shall be concluded on the basis of fair trade, and any profits or financial position of the Target Company shall not be affected by any contract or arrangement that has not been concluded on the basis of fair trade.





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12. Related Party Transaction

The transaction (including but not limited to occupied fund, financing providing, procurement, license, credit and debt, etc.) between the Target Company and each Warrantor and its related party has been adequately disclosed. In other case, there shall be no other transaction between the Target Company and each Warrantor and its related party. Commercial terms concerning related party transaction between the above mentioned parties are fair and just, without situations damaging the interest or increasing the burden of the Target Company.

13. Environment

The Target Company does not have any major violation to applicable laws or regulations concerning environmental protection. The Company has always substantially observed applicable international conventions/treaties, international standards, international industrial codes and applicable laws, regulations, industrial codes, guidelines, documents and standards related to environmental protection issued by the local government of the operation place. In addition, the Target Company has never received any related complaints, protests, warnings or punishments, etc.

14. Tax

- 14.1 The Target Company has gone through all the related tax registrations according to related laws and the requirement of the tax authority. The Company has gone through the tax declaration in time and paid adequate tax timely. There is no tax dispute, nor are there any other cases that are likely to cause any punishment to the Target Company. As regarded to the taxable payment or the possible tax ability of the Target Company, it has adequately made provision or published in items of the account.
- 14.2 Target Companies have paid all the due taxes payable, tariff and levy. As far as each Warrantor concerns, or after appropriate inquiry or with discreet obligation, these Companies shall be known as companies under no investigations from tax authorities.

15. Full Disclosure

- 15.1 After the Buyer expresses the intention to buy share from the Seller or subscribes any shares, for all information provided by the Warrantor to the Buyer or to any of its representatives, or provide by other parties representing Warrantors to the Buyer or to any of its representatives, these information in all aspects shall be true and accurate. In addition, there shall be no facts or terms not in written form provided to the Buyer or to any of its representatives that make the above mentioned information untrue or misleading.
- 15.2 All Warrantors do not know any truth or situations related to them or their target businesses that may cause major adverse impact, or any truth or situations yet to be disclosed in any document that may influence the Buyer's decision to buy shares from the Seller or subscribe shares according to clauses hereof after appropriate estimation.
- 15.3 For all representations and warranties of each Warrantor hereunder, and those provided or to be provided to the Buyer according to the Agreement, or those related to transactions proposed hereunder, there contains no false statement with any material facts and will not contain any false statement with material facts. In addition, all above mentioned representations and warranties do not and will not miss any material facts that may make the statement thereunder misleading.



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## Part II Payment Guarantee of the Remaining Consideration

1. Target Business and Target Asset
  - 1.1 Before the Payment Date of the Remaining Consideration, the Target Business is mainly operated in Taiwan, Russia and Brazil. No business is operated in other places.
  - 1.2 In completing the transaction, before transferring the Target Business and all Target Assets necessary or related to the operating of Target Business to the Hong Kong Company and WFOE, each Warrantor is the only legal title holder of the Target Business and Target Asset, with no encumbrance attached, including the right to file a lawsuit against infringement act.
  - 1.3 After transferring the Target Business and Target Assets to the Hong Kong Company and WFOE, assets (including Target Assets) legally held, occupied or controlled by each group company are under fine condition with no encumbrance attached. These assets constitute the necessary asset, property and right of the group company to conduct the Target Business. Only based on these assets, the Target Business can be operated with the Target Asset in the form and scale of the Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea before the Payment Date of the Remaining Consideration.
2. License
 

Every group company has legally and effectively operated the Target Business in major operation places (namely Taiwan, Russia and Brazil) without violating any applicable laws. As far as the Seller knows, no possible fact may make the local target business operation of the group company illegal or fail to guarantee the Target Business to be further operated in the way and scale of the time before the Signing Date of each Warrantor.
3. Intellectual Property and Business Secrets
  - 3.1 In carrying out the transaction, before transferring intellectual property to the Hong Kong company and WFOE, each Warrantor is the only legal title holder of intellectual property, with no encumbrance attached, including the right to file a lawsuit against infringement act. There is no pending or intended appeal questioning the effectiveness, enforceability, scope, clauses or other aspects of any intellectual property. Moreover, no intellectual property is wholly or partially identified as invalid or unenforceable due to any reason in any appeal.
  - 3.2 After transferring intellectual property to the Hong Kong Company and WFOE, every group company legally holds intellectual property, with no encumbrance attached. The held intellectual property is adequate to enable every group company after the Payment Date of the Remaining Consideration according to the Closing Date to operate the Target Business with the intellectual property in the state when the transaction is carried out before the intellectual property is transferred to the Hong Kong Company and WFOE.
  - 3.3 Each Warrantor has taken appropriate measures to protect the confidentiality and value of all of its business secrets. Unless as specified in valid, proper and unviolated confidentiality and/or license agreement, no one has used, disclosed or discovered any business secret related to the Target Business. For their own interests (as appropriate), related employees and consultants have signed the Intellectual Property Confidentiality Agreement. According to the Agreement, every employee and consultant has transferred every intellectual property to the Target Group (if any) and agrees to keep the confidentiality of all business secrets.
  - 3.4 Each Warrantor or any previous owner of the intellectual property has not received any notification of any threatened-to-be, pending or ongoing appeal concerning intellectual property or other actual or claimed intellectual property violation involving any third party. In addition, each Warrantor or any previous owner does not know any reason to anticipate any fact or situation that may cause any appeal of this kind.



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- 3.5 Each Warrantor or any previous owner of the intellectual property has never authorized a third party of the right to use any intellectual property or other rights.
- 3.6 All reward and payment to the inventor of any intellectual property required by laws or other reward or payment to the creator or designer has been fully paid to the related inventor, designer and creator.
- 3.7 There is no third party registering or using other intellectual property (including the trade mark) related to any Target Business (whether the intellectual property has been registered or not, registration application included), or registering or using any domain name with the same or similar name of the ones owned or used by the Target Company, or used in other ways of business (including the Target Business).
4. Information Technology
  - 4.1 Each Warrantor shall provide all information technology (including but not limited to software under developing), statistics of registered players and all details of the historic operation data used by the Target Business to the Target Group on or before the Payment Date of the Remaining Consideration. Afterwards, the Target Group becomes the only legal and beneficial owner of the corresponding information technology with no encumbrance attached under this situation, or the Target Group becomes the legal licensee of this information technology.
  - 4.2 All information technology of the Target Business is in fine working condition and is maintained according to good industrial conventions.
  - 4.3 Each Warrantor has provided the details of all agreements and arrangements related to the information technology established by the Target Business or from which they benefit on or before the Payment Date of the Remaining Consideration.
  - 4.4 Any information technology of the Target Business shall not be the subject of any lawsuit or other disputes or claim for rights.
  - 4.5 The Target Business has not encountered any suspension in business or operation because of the following terms: (i) any security flaw related to any information technology, (ii) any breakdown of any information technology (whether it is caused by any flaw, virus, defect or other reason), under capacity or other sub-standard performance, or (iii) any information technology breakdown, suspension or operation with defects due to the occurrence or treatment of any date. There shall be no situation that may or is estimated to cause any suspension of this kind.
  - 4.6 All necessary or needed information technology or business information of the Target Business shall not be directly or indirectly impaired because of the transaction proposed hereunder.
  - 4.7 Any information technology used by each Warrantor in this Target Business did not violate or use without authorization the information technology of any third party twelve (12) months before the Payment Date of the Remaining Consideration.
5. Information Saved by the Server
 

All servers' information of each Warrantor in the Target Business is true, accurate and complete at the payment time on the Payment Date of the Remaining Consideration and the information is not mastered or known by any third party except each Warrantor.
6. Material Contract
 

Regarding the Target Business, each Warrantor remains in fine relationship with related users, show hosts, distributors, servers and broadband providers and other stake holders to this business. Therefore the continuity of the Target Business can be maintained without service suspension because of the transfer of contract or the change of servers.



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7. User

The Target Group has not received any notification and no party has any reason to believe that in any time after the Payment Date of the Remaining Consideration the Target Group will be unable to get steady income from the current users of the Target Business, or the number of future users of the Target Business will have a great decrease comparing with the previous income.

8. Employment

Each Warrantor has appropriately terminated the employment contract with employees in the Target Asset on or before the Payment Date of the Remaining Consideration and has paid all fees related to the termination of employment contract including economic compensation.

9. Full Disclosure

9.1 After the Buyer expresses the intention to buy share from the Seller or subscribes any shares, for all information provided by the Warrantor to the Buyer or to any of its representatives, or provide by other parties representing Warrantors to the Buyer or to any of its representatives, these information in all aspects shall be true and accurate. In addition, there shall be no facts or terms not in written form provided to the Buyer or to any of its representatives that make the above mentioned information untrue or misleading.

9.2 Each Warrantor does not know any truth or situations related to them or their Target Businesses that may cause major adverse impact, or any truth or situations yet to be disclosed in any document that may influence the Buyer's decision to buy shares from the Seller or subscribe shares according to clauses hereof after appropriate estimation.

9.3 For all representations and warranties of each Warrantor hereunder, and those provided or to be provided to the Buyer according to the Agreement, or those related to transactions proposed hereunder, there contains no false statement with any material facts and will not contain any false statement with material facts. Also, all above mentioned representations and warranties do not and will not miss any material facts that may make the statement thereunder misleading.

**Part III Warrantors' Guarantee Concerning Target Business and Target Asset**

1. Compliance with Laws

1.1 The operation of Target Business and Target Asset does not violate and has never violated any applicable laws, including national laws and regulations and local rules and regulations applied to the Target Business and Target Assets issued in the judicial field of the Target Business.

1.2 Except items to be discussed herein, the completion of the transaction hereunder will not (i) constitute the breach of any clause of any agreement related to the Target Business and Target Asset, or bring any right to cease, terminate or bring forward any right or obligation about the Target Business or Target Asset under any clause of any contract, or lead to the loss of any interest of the Target Business and Target Asset under any clause of any contract, or lead to any increase of the current effective interest rate of any debt related to the Target Business and Target Asset; (ii) make any encumbrance out of the Target Asset; or (iii) make it impossible or difficult for the Hong Kong Company and WFOE to own and operate the Target Business and Target Asset in its intended way.

1.3 All contracts related to the Target Business and Target Asset are effective and constitute the binding obligation of contracting parties. At the same time all major aspects of the contract shall be observed. No cease notification or notification of termination intention has been received.



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- 1.4 None of the following events has existed or occurred (whether notification or passage of time is needed): (i) that may constitute or lead to the violation or failure to observe any applicable laws of the Target Business or Target Asset, or (ii) that may lead the Hong Kong Company and WFOE obliged to perform any remedial action or assume the whole or partial cost of the remedial action. In addition, concerning the Target Business and Target Asset, each Warrantor has not received from any government authorities (x) any actual, alleged, possible or potential breach or failure to observe any applicable laws, or (y) any actual, alleged, possible or potential remedial action or any notification or other message (whether in oral or written form) to assume the whole partial cost of the remedial action.
2. No Appeal or Lawsuit
- 2.1 There is no pending or threatened-to-be issued appeal or lawsuit that is issued against or influences the Target Business or Target Asset. Neither the Target Business nor the Target Asset is involved in any form in the appeal that has already or is predicted to bring adverse influence separately or collectively. There is no fact or situation that may lead the appeal to investigation and punishment.
- 2.2 There is no pending judgment, court order or arbitral decision against the Target Business and Target Asset, nor does any detention, execution or procedure of the above mentioned events exist.
3. Financial Data
- 3.1 Financial data shall be accurate and complete, reflecting the actual situation and financial condition and value of the Target Business and Target Asset on corresponding date in a true, comprehensive and just manner;
- 3.2 Financial data is prepared according to the US Generally Accepted Accounting Principle and/or Chinese Accounting Standards;
- 3.3 Financial data have disclosed the Target Asset, the value of the Target Business for the purpose of transaction and other significant items in an accurate, complete, true, comprehensive and just manner.
4. Events After September 30, 2013
- 4.1 From September 30, 2013, except those for the purpose of normal operation, disclosed in the financial data or required by the transaction,
  - (a) all Target Businesses shall be carried out and/or expanded according to the normal operation practice and/or the actual situation, so as to maintain its sustainability, without changing any management or operation form of its business, undertaking or asset, except the change in accordance with the fixed conventional way and the expansion of business based on the actual situation;
  - (b) There isn't any event that has any major adverse impact on the Target Business and Target Asset;
  - (c) The Target Business has paid no capital expenditure over RMB 300,000 or made any capital commitment over RMB 300,000 outside the normal operation process;
  - (d) The Target Business has not set, arose, assumed or encountered any debt or guarantee;
  - (e) The Target Business has no (i) reconciliation, or offered or proposed reconciliation; (ii) lawsuit, investigation, arbitration, procedure or other claim for rights; or (iii) lawsuit, investigation, procedure or dispute related to the transaction proposed hereunder;



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- (f) The Target Business is not sold, rented or transferred to others, or is set or brought to any encumbrance;
  - (g) The Target Business does not violate any clause or regulation of any contract or any applicable law.
5. Real Estate
- 5.1 Each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) enjoys or has the legal and beneficial ownership and other rights or interests over any real estate (if any) needed for its operating Target Business and Target Asset.
- 5.2 Every lease shall constitute the entire agreement of the corresponding real estate with each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) as a party. The authentic and complete copy of every lease, attached with all amendment, revision and correction, has been submitted to the Buyer. Every lease validly exists. It can be implemented to every party according to its clauses and every lease has gone through necessary registration and filing. On the Closing Date or the Payment Date of the Remaining Consideration, all prerequisites for the implementation of every lease have been satisfied. Each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) have accepted and actually occupied the corresponding real estate without subleasing, releasing or pledging its leasehold interest.
- 5.3 Each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) have always timely paid any rent or other expenditures and costs according to the lease. Under any lease, there is no violation or violation event of each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) that has not been remedied or is still under investigation. Also there is no event that may constitute violation or violation event upon the issuance of notification or along the passage of time or both, nor does there exist any pending or possible expropriation, confiscation, dispute, claim for rights, requirement or other similar procedure that is related to or may have adverse effect on the consistent use or ownership of any lease.
- 5.4 The landlord of every lease has the full ownership of real estate under the lease, with property defect not attached. Every real estate under any lease is in all aspects in accordance with laws and suitable for the business operation of each Warrantor (before the completion of the reorganization plan) and the Hong Kong company and WFOE (after the completion of the reorganization plan). When the use, occupation and operation of every lease and each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) follows the way the real estate under the lease is currently used, occupied and operated, the applicable laws concerning the construction, planning, fire protection, partition and the use of the lands will not be violated.
6. Material Contracts
- 6.1 Unless otherwise stipulated in the Agreement, there is no claim in any agreement, document or arrangement for or related to the Target Business and Target Asset, the failure to observe or the breach of which may lead to major adverse impact on the whole Target Business and target asset. Nor will there be any possibility or any situation possible for the claim of this kind.
- 6.2 On the actual knowledge of each Warrantor or what shall be reasonably known after proper inquiry or doing duty of care, all involved parties under the Agreement related to the Target Business do not violate the Agreement or the obligation hereunder.





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- 6.3 On the actual knowledge of each Warrantor or what shall be reasonably known after proper inquiry or doing duty of care, there is no offer, bid or similar event that will have great adverse impact on the Target Business and Target Asset.
- 6.4 The Target Business does not establish or assume any contract, transaction, arrangement or responsibility of the following kind (except that such contract, transaction, arrangement or responsibility is still effective and/not completed on the Closing Date or the Payment Date of the Remaining Consideration, and the amount of the contract, transaction, arrangement or responsibility exceeds RMB 300,000, but the obligation of each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan) under the contract, transaction, arrangement or responsibility is accurately reflected in the financial data): the nature is special or abnormal or beyond the scope of normal business.
- 6.5 All contracts or arrangements related to the Target Business (such contract or arrangement is still effective or not completed on the Closing Date or the Payment Date of the Remaining Consideration) are established on the basis of fair trade. In addition, the profit or financial condition of any Target Business is not affected by any contract or arrangement that is not established on the basis of fair trade.
7. Employment
  - 7.1 On the Signing Date, Closing Date and the Payment Date of the Remaining Consideration of the Agreement, there is no requirement, claim for compensation, reimbursement (whether according to applicable laws or others) or other payment from the current or former employees, directors or other administrative staff of the Target Business or their family inheritors or family members.
  - 7.2 On the Signing Date, Closing Date and the Payment Date of the Remaining Consideration of the Agreement, employees of the Target Business are not involved in any trade or industrial dispute or any fact that may be related to any industrial dispute. The fact is known or become known after proper query.
  - 7.3 On the Signing Date, Closing Date and the Payment Date of the Remaining Consideration of the Agreement, unless otherwise stipulated in the applicable laws of the related jurisdiction or disclosed in the financial data, former or current administrative staff or employees of the Target Business or their family members have no other retirement payment, annuity, pension or similar welfare, nor do they be planned to enjoy this welfare in the future.
  - 7.4 Except the transaction proposed hereunder, employees of the Target Business are not set to have share option plan, share incentive plan or similar plans.
  - 7.5 On the Signing Date, Closing Date and the Payment Date of the Remaining Consideration of the Agreement, excepting working for each Warrantor (before the completion of the reorganization plan) and the Hong Kong Company and WFOE (after the completion of the reorganization plan), employees of the Target Business do not engage in business the same as or similar to the Target Business, unless the one disclosed by each Warrantor in the disclosure letter of the Agreement.
8. Tax
  - 8.1 Tax related to the Target Business has gone through all the related tax registrations according to related laws and the requirement of the tax authority and paid tax in full timely. There is no tax dispute, nor are there any other cases that are likely to cause any punishment to the Target Company. As regarded to the taxes payable or the possible tax ability of the Target Business, it has adequately made provision or disclosed in the financial data.
  - 8.2 Target Companies have paid all the due taxes payable, tariff and levy. As far as each Warrantor concerns, or after appropriate inquiry or with discreet obligation, these Companies shall be known as companies under no investigations from tax authorities.





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#### Part IV Representations and Warranties of Each Warrantor

1. Establishment, Good Credit Standing and Qualification

Each Warrantor is (1) a valid existing limited company with good credit standing, legally established according to the local applicable laws. Its establishment has obtained the approval of all government authorities (if necessary); (2) has all necessary rights and authorization to own and operate its property and develop its business, and sign, deliver and perform the Agreement and the transaction proposed hereunder; (3) has the qualification for trade transaction; has all necessary license and qualification for the business operation and owns good credit standing in every jurisdiction calling for the due qualification; and (4) has always developed its business legally since its establishment.

2. Authorization

- 2.1 Each Warrantor has taken all necessary measures to make it possible to authorize, sign and deliver the Agreement and perform obligations hereunder. The Agreement and other agreement and/or instrument that make each Warrantor a party accordingly constitute its effective and legally binding obligations which can be implemented according to its clauses.
- 2.2 When signing, delivering or performing the Agreement or completing the transaction proposed hereunder, each Warrantor does not need to get other extra permission from any person except those already obtained on the Closing Date and/or the Payment Date of the Remaining Consideration.

3. Seller's Shares and Share to Be Subscribed

- 3.1 Seller's Shares bought by the Buyer (i) have been officially issued and paid in full amount, (ii) shall transfer to the Buyer on the Closing Date the ownership which is partially effective to the Seller's Shares with no alienation restriction and other encumbrance attached. And all rights and interests attached to the Seller's Shares shall be transferred.
- 3.2 According to the clause hereof, the Target Company shall transfer the ownership of the shares to be subscribed which is appropriately effective with no alienation restriction and other encumbrance attached. And all rights and interests attached to the share shall be transferred.

4. Non-violation

Each Warrantor's signing, delivering and performing of the Agreement or completing of the transaction proposed hereunder will not (i) constitute conflict against any applicable laws; (ii) constitute the violation of any clause of any contract, or bring any right to cease, terminate or bring forward any right or obligation under any clause of any contract, or lead to the loss of any interest of the Target Business and Target Asset under any clause of any contract, or lead to any increase of the current effective interest rate of any debt related to the Target Business and Target Asset; or (iii) make any encumbrance out of any asset or property of each Warrantor (unless otherwise clearly agreed in the transaction document of each party).

5. Insolvency

Each Warrantor will not or has no reason to believe that there will be insolvency or unpayable debt in the foreseeable future according to applicable laws. No compromise with the creditor or other related legal process, or any liquidation, bankruptcy or other dissolution procedure involving each Warrantor exists or is believed to take place in the foreseeable future. In addition, as far as each Warrantor knows, there isn't any event that may trigger this legal process according to applicable laws.



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6. No Claim or Lawsuit

There is no pending or threatened-to-be claim related to any aspect of the Target Group or Target Business or Target Asset, against or influencing each Warrantor or its related party.

**Part V Representations and Warranties of the Buyer**

1. Establishment, Good Credit Standing and Qualification

The Buyer is a valid existing company with good credit standing appropriately established according to applicable laws of British Virgin Islands. The Buyer has all necessary corporate rights and authorization for signing and delivering the Agreement and performing the transaction hereunder.

2. Authorization

The Buyer has the full right and authorization to establish this Agreement. When the signing and delivery of the Agreement is valid, the Agreement constitutes valid and legally binding obligations which can be implemented accordingly.

3. Non-violation

The Buyer's signing, delivering and performing of the Agreement or completion of the transaction hereunder will not (i) constitute conflict against any applicable laws, whether along with the passage of time or upon notification; (ii) constitute dispute against any applicable laws; or (iii) constitute the violation of any clause of any contract, or bring any right to cease, terminate or bring forward any right or obligation under any clause of any contract, or lead to the loss of any interest of the Buyer under any clause of any contract.



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### Annex III Reorganization Plan

- Step 1: The Seller establishes the Target Company in the British Virgin Islands according to the local laws five (5) business days after the Signing Date.
- Step 2: The Target Company invests and establishes a limited company ("the Hong Kong Company") in Hong Kong according to the laws of Hong Kong.
- Step 3: The Hong Kong Company invests and establishes a wholly foreign owned enterprise (WFOE) in Beijing, China according to the law of the PRC.
- Step 4:
- (A) The Hong Kong Company accepts the Target Business and Target Asset from the Seller and Kunlun Korea, including the listed asset and contract in Part III of Annex IV and the listed asset and employees in Part IV of the same Annex; and
  - (B) WFOE transfers the Target Business and Target Asset from Kunlun Beijing and Kunlun Guangzhou, including the listed asset and employees in Part I of Annex IV and asset and employees in Part IV of the same Annex.
  - (C) According to items (A) and (B), the Hong Kong Company and WFOE keep the consideration of the corresponding Target Business and Target Asset in the form of accounts payable into the financial statements of Hong Kong Company and WFOE ("Amount of Accounts Payable"). In the process of reorganization, no actual payment will be performed.



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**Exhibit 4.89**  
**English Translation**

**Supplementary Agreement to Investment Agreement**

This Supplementary Agreement to Investment Agreement (hereinafter referred to as “**the Supplementary Agreement**”) is entered into in Beijing, the People’s Republic of China on the day of December 24, 2013 (hereinafter referred to as “**Signature Date**”) by the following parties:

- (1) Koram Games Limited, a company duly incorporated and validly existing under the laws of Hong Kong, with its registration No. as 1415564 and registered address located at Suite 1203, 12th Floor, Ruttonjee House, 11 Duddell Street, Central, Hong Kong (“**Seller**”);
- (2) HEROIC VISION HOLDINGS LIMITED, a company duly incorporated and validly existing under the laws of British Virgin Islands, with its registration No. as 1795916 and registered address located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (“**Buyer**”);
- (3) Beijing Kalends Technology Co., Ltd., a limited liability company duly incorporated and validly existing under the laws of PRC, with its registration No. as 110108010907077 and registered address located at 605E, Tower B, No. 118 Zhichun Road, Haidian District, Beijing (“**Kunlun Beijing**”) and the legal representative is Zhou Yahui;
- (4) Guangzhou Kunlun Online Information Technology Co., Ltd., a limited liability company duly incorporated and validly existing under the laws of PRC, with its registration No. as 440106000147934 and registered address located at Third Floor, No. 44-46 Jianzhong Road, Tianhe District, Guangzhou, Guangdong Province ( “**Kunlun Guangzhou**”) and the legal representative is Zhou Yahui;
- (5) Kunlun Korea Co., LTD., a company duly incorporated and validly existing under the laws of Korea, with its registration No. as 2148870398 and registered address located at 10F823Bldg, 823-16 Yeoksam-Dong, Gang-nam Gu (“**Kunlun Korea**”).

For the purpose of this Agreement, the Parties abovementioned are called collectively as the “**Parties**” and respectively as a “**Party**”. **Seller, Kunlun Beijing, Kunlun Guangzhou and Kunlun Korea** are called collectively as “**Warrantors**” and respectively as a “**Warrantor**”.

Whereas, the **Parties** executed the *Investment Agreement* (hereinafter referred to as “**Original Agreement**”) concerning the issues on investment target company on November 19, 2013, Now, the Parties intend to make amendments to the Original Agreement and have agreed to make the following Supplementary Agreement upon consensus through negotiation:

1. Unless otherwise defined herein, the terms and expressions used in this Supplementary Agreement shall have the meanings set forth in Original Agreement.
2. Delete Article 1.1.3 set forth in Part 1 of Annex 4 and Article 1.1.1, Domain Name of Part 4 of the Original Agreement and modify the content aforesaid into the content set forth in Annex 1 of this Supplementary Agreement.



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3. Add Article 5.10.4 into Article 5.10 of the Original Agreement:  

Within twenty (20) Business Days of the Payment Date of the remaining consideration, the domain name in the target asset (please refer to Annex 2) held by Kunlun Beijing and Kunlun Korea respectively but not transferred into Hong Kong Company or WFOE before the Payment Date of consideration, shall be registered in the name of Hong Kong Company or WFOE. In addition, the Parties guarantee individually and jointly that the target business shall still be in normal operation before the domain name in the target asset was transferred into Hong Kong Company or WFOE and the user of target business shall be provided with normal business services without interruption and steadily; moreover, while transferring the domain name, the normal operation of target business shall not be affected by such kind of act and shall remain normal as before.
4. Delete the content of Employee set forth in Article 1.2 of Part 1 and Article 1.2 of Part 2 of Annex 4 provided in Original Agreement and replace them respectively with the content of Employee set forth in Article 1.2 of Part 1 and Article 1.2 of Part 2 of Annex 3 of the Supplementary Agreement respectively.
5. Delete Article 1.1, Asset of Part 3 of Annex 4 set forth in Original Agreement.
6. Delete the definition part of “Restricted Employee” set forth in Annex 1 of the Original Agreement and replace it with the following articles:

“Restricted Employee” Refers to the target business employee as well as the following personnel:

- \* (ID number: \*)
- \* (ID number: \*)
- \* (ID number: \*)
- \* (ID number: \*)“

7. Delete the definition part of “Target Business Employee” set forth in Annex 1 of the Original Agreement and replace it with the following clauses:

“Target Business Employee” Refers to the employee set forth in Article 1.2 of Part 1 and Part 2 of Annex 4.”

8. In terms of pre-condition of the payment of the remaining consideration provided in Article 3.3.1 and 3.3.15 of Original Agreement, the Parties agree that the labor contract with \* (Chinese ID number: \*), who is subordinate to the Base Research and Development Department of Kunlun Guangzhou, and the Confidentiality Agreement as well as Non-compete Agreement shall be executed as soon as possible after the payment of the remaining consideration. Such executions shall not be deemed as a pre-condition. While the Original Agreement and any terms and conditions relating to the modification of this Article, including but not limited to Article 3.3.1 and Article 3.3.15 of Original Agreement shall be deemed to be modified and adjusted with this Article accordingly.
9. Unless otherwise modified or supplemented herein, the Original Agreement shall remain in full force and effect.

**The symbol “\*” in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.**



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10. The Supplementary Agreement shall be governed by and construed in accordance with the laws of Hong Kong. Any disputes, controversies or claims arising out of or relating to this Supplementary Agreement or the interpretation, violation, termination or validity of this Supplementary Agreement shall be resolved on the basis of Article 12.4 set forth in Original Agreement.
11. The Supplementary Agreement shall become effective as of the signing date by the duly authorized representatives of the Parties (the Parties hereto established in China shall affix their official seals). The Supplementary Agreement and Original Agreement shall constitute one and the same instrument upon the effective date of this Supplementary Agreement, in case of any conflict arising between this Supplementary Agreement and Original Agreement, the former shall prevail.
12. The Supplementary Agreement is made in Chinese and may be executed in one copy or any number of counterparts, each of which shall be deemed as an original and all of which shall constitute one and the same instrument.

*[No Text Below]*



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**IN WITNESS WHEREOF**, the Parties hereto have executed this Agreement as of the day and year first above written by duly authorized representatives of each party and the Parties hereto duly established in China shall affix their official seals.

Koram Games Limited

Signature: /s/ Zhou Yahui

Name: Zhou Yahui

HEROIC VISION HOLDINGS LIMITED

Signature: /s/ Wang Tao

Name: Wang Tao





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Beijing Kunlun Technology Co., Ltd. (seal)

Signature: /s/ Zhou Yahui

Name: Zhou Yahui

Guangzhou Kunlun Online Information Technology Co., Ltd. (seal)

Signature: /s/ Zhou Yahui

Name: Zhou Yahui

Kunlun Korea Co., LTD

Signature: /s/ Zhou Yahui

Name: Zhou Yahui



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Exhibit 4.90  
English Translation

Koram Games Limited  
  
And  
  
HEROIC VISION HOLDINGS LIMITED  
  
And  
  
TalkTalk Limited

Shareholder Agreement

Executed on November 19, 2013



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#### Recitals

This Shareholder Agreement (“the Agreement”) is entered by and among the following parties in Beijing, China on November 19, 2013:

- (1) Koram Games Limited, a limited liability company established and existing under the laws of Hong Kong (registration number: 1415564), with its registered address located at Suite 1203, 12<sup>th</sup> Floor, Ruttonjee House, 11 Duddell Street, Central, Hong Kong (“Kunlun”);
- (2) HEROIC VISION HOLDINGS LIMITED, a limited company established and existing under the laws of British Virgin Islands (registration number: 1795916), with its registered address located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (“Heroic Vision”);
- (3) TalkTalk Limited, a limited company established and existing under the laws of British Virgin Islands (registration number: 1799119), with its registered address located at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (“the Company”).

The above parties are hereinafter referred to as “the Parties” collectively, and a “Party” separately.

#### Whereas,

- (1) The Parties agree to conclude the Agreement, clarifying the relations between the Parties, as Shareholders of the Company, and relevant terms and conditions regarding the Company’s management and operation.
- (2) The Company agrees to become a Party hereto to confirm the terms and conditions set forth herein and to abide by the matters related to the Company hereunder.

Therefore, the Parties, through negotiation and conclusion of a consensus, agree on the following terms and conditions which are binding on the Parties:

### Article 1 Definitions and Interpretation

#### 1.1 Definitions

Unless otherwise specified in the context, the terms in bold letters herein shall have corresponding meanings assigned to them in Annex 1. Unless otherwise defined in Annex 1, the terms in bold letters herein shall have corresponding meanings assigned to them in Investment Agreement.

#### 1.2 Interpretation

- 1.2.1 Any reference to the Agreement includes annexes and appendixes that are inseparable from the Agreement. “Hereof”, “hereunder”, “herein” and other words with similar meanings shall refer to the entire Agreement other than some article, schedule, annex or appendix. Any reference to any document (including the Agreement) shall be interpreted as the document amended, consolidated, supplemented, updated or superseded from time to time. Unless otherwise specified, (i) any annex or appendix mentioned shall refer to corresponding annex or appendix hereto, and (ii) any article mentioned shall refer to corresponding article in the main body of the Agreement.



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- 1.2.2 “Including” used herein shall be interpreted as “including but not limited”.
- 1.2.3 Any reference to any Party to the Agreement or any other agreement or document shall be interpreted as including such Party’s successor or authorized transferee.
- 1.2.4 “Person” shall include natural person, business office, company, government authority, joint operational project, partnership, committee, unincorporated organization, trust, corporation or other entity (regardless of independent legal entity status).

## **Article 2 Shareholding Ratio of Shareholders**

- 2.1 On the Closing Date, the Company has issued 10,000 shares, which are all ordinary shares with 1.00 USD per share as par value.
- 2.2 On the Closing Date, shareholding ratio of the Shareholders is listed as follows, in accordance with the Investment Agreement:
  - 2.2.1 Heroic Vision, holding 6,250 ordinary shares in the Company, with shareholding ratio of 62.5%;
  - 2.2.2 Kunlun, holding 2,250 ordinary shares in the Company, with shareholding ratio of 22.5%;
  - 2.2.3 The Company, holding 1,500 ordinary shares in the Company (as treasury shares), with shareholding ratio of 15%.

## **Article 3 Company Business**

- 3.1 Except for being approved by Shareholders holding over 50% of the voting right, business of the Group shall be limited within the scope of Group business.
- 3.2 Group business shall be carried out for maximization of the Company’s interests, and the Company shall make every reasonable effort to maintain, improve and expand Group business through means suitable for the approved business plans.
- 3.3 The Parties agree that their respective rights in the Company shall be governed by the Agreement and the Articles of Association. Shareholders and the Company agree to comply with the terms hereunder and other relevant provisions, and all terms and conditions in the Articles of Association may be enforced to the Company and its Shareholders.
- 3.4 Except for being approved by Shareholders holding over 50% of the voting right, all shares and/or equity interest of the Subsidiary Company of the Company shall be held, directly or indirectly, by the Company.

## **Article 4 Promotion Resources of Website 17173**

Heroic Vision agrees to make every reasonable effort to provide the Group with promotion resources of the subordinate Website 17173, and to utilize various strengths to play a role of integration.

## **Article 5 Shareholders’ Meeting**

- 5.1 The Company has its Shareholders’ Meeting. Shareholders’ meeting shall be governed by Shareholders, exercising their portion of voting right in accordance with their shareholding ratio.
  - 5.1.1 Resolutions with respect to the following matters shall take effect only upon the approval of Shareholders holding over 66.7% of the issued shares:
    - (a) The Company’s capital increase, issuance of shares for capital increase;



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- (b) Any form of the Company's merger, division, transformation or dissolution, liquidation; and
- (c) Any company's becoming a Subsidiary Company of the Company due to the Company's acquisition of such company's issued shares or any part of its capital and business.
- 5.1.2 Unless otherwise stipulated in any governing law and under Article 5.1.1, in case of resolution made by the Shareholders' meeting on any other matters, such resolution shall take effect only upon approval of Shareholders holding over 50% of the issued shares.
- 5.1.3 Shareholders' meeting shall be governed by Shareholders, exercising their portion of voting right in accordance with their shareholding ratio.
- 5.2 Each shareholders' meeting (regardless of formal or interim meeting) shall be informed to each Shareholder, via written or e-mail, by the Chairman in ten (10) business days preceding the intending meeting, specifying the date, time and location thereof ("Meeting Notice"). If all Shareholders agree to a relatively short notice period, then the meeting with which such notice period is applied shall be considered as convened appropriately.
- 5.3 Shareholder who cannot attend shareholders' meeting shall entrust an agent to attend the meeting prior to the intended time of such meeting, and the agent may exercise power specified in the power of attorney.
- 5.4 Shareholders can use telephone, teleconference or similar equipments to attend shareholders' meeting, and the shareholders' meeting can convene meeting via the above means. It shall be considered that the Shareholder attends the meeting in person on the condition that Shareholders are capable of sending and receiving opinions via interaction methods.
- 5.5 A written resolution signed by all Shareholders qualified to attend the meeting and voted shall be considered as having the same force and effect as resolution passed in shareholders' meeting duly convened and held. Any Shareholder, receiving the written resolution issued by the Board, shall approve or reject such written resolution in ten (10) business days upon receipt.
- 5.6 The Chairman shall be the president of Shareholders' Meeting. If the Chairman is unavailable or fails to (or refuses to) perform its responsibilities, then the Shareholder attending and holding the most shares is entitled to appoint a chairman to perform corresponding responsibility in such meeting.

## Article 6 Board of Directors

- 6.1 Establishment
 

The Company has a Board of Directors, subject to Article 5.1.1, which shall be responsible for overall instruction, supervision, management and strategies of the Company.
- 6.2 Composition of the Board of Directors
  - 6.2.1 The Board of Directors of the Company is constituted by five (5) directors, and three (3) of which are assigned by Heroic Vision, the other two (2) are assigned by Kunlun and Management Shareholders, including:
    - (a) From the Closing Date to the time that any Management Shareholder acquires the Company's shares according to share option incentive plan of Management Shareholders, Kunlun is entitled to appoint two (2) directors to the Company and one (1) of them must be an employee from management staff of the Company; and
    - (b) From the time that any Management Shareholder acquires the Company's shares according to share option incentive plan of Management Shareholders, Kunlun is entitled to appoint one (1) director, and the Management Shareholders are entitled to appoint one (1) director.



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- 6.2.2 The Company has one (1) Chairman, who shall be appointed directly by Heroic Vision.
- 6.2.3 Alternate director: any director, with written consent by the Shareholder appointing him/her, may entrust any person (which can be one director of the Company) to be his/her alternate director at any time via written notice to the Company. The alternate director has all rights, privileges and power granted to him/her by the appointing director when acting on such director's behalf, but shall be subject to various provisions concerning directors in the Articles of Association and the Agreement. Any director may terminate his/her appointment of alternate director at any time via written notice to the Company and Shareholder appointing such director.
- 6.2.4 Shareholders undertake that they shall ensure the realization of the right of appointing director under Article 5.2 hereof by means of affirmative vote in shareholders' meeting or executing Shareholders' written resolution.
- 6.3 Meeting of the Board of Directors and the Quorum
- 6.3.1 Meeting of the Board of Directors shall be convened quarterly. Interim meeting of the Board may be convened upon written proposal of two (2) directors. Unless otherwise stipulated in any governing law, any resolution made with respect to matters under Article 5.1.1 during the meeting of the Board of Directors shall be passed on the condition of approval by over 2/3 of the directors of the Board; resolution made with respect to other matters shall be passed on the condition of approval by over 50% of the directors of the Board.
- 6.3.2 In order to achieve the quorum, at least three (3) directors shall attend in person or appoint alternate director to attend the board meeting held each time. Resolutions made in board meeting without sufficient quorum are invalid.
- 6.3.3 Notice, agenda and relevant materials of the board meeting shall be delivered to each Shareholder at least in ten (10) days preceding such meeting. Meeting notice shall include the date, time, place, agenda and any relevant materials. If all Shareholders agree to a relatively short notice period, then the meeting with which such notice period is applied shall be considered as convened appropriately. Unless approved by all directors, agenda already delivered to directors may not be modified or added.
- 6.3.4 Director may attend the board meeting and voting in person or by entrusting alternate director.
- 6.3.5 Directors can use telephone, teleconference or similar equipments to attend the board meetings, and the Board of Directors can convene meeting via the above means. It shall be considered that the director attends the meeting in person on the condition that directors are capable of sending and receiving opinions via interaction methods.
- 6.3.6 A written resolution executed by all directors shall be considered as having the same force and effect as resolution passed in the board meeting duly convened and held. Any director, receiving the written resolution proposed by the Company, shall approve or reject such written resolution in ten (10) business days upon receipt.
- 6.3.7 Subject to good faith obligation and compliance with governing laws, a director may inform the Shareholder appointing such director about all material matters in relation to Company Business and events, and each Shareholder receiving such information guarantees and agrees that such information is confidential information.

#### **Article 7 Board of Directors and Management of the Group**

- 7.1 Composition of the board of directors of other Group Companies shall be the same as the Board of Directors of the Company. Each board meeting of Group Companies shall be held in accordance with the provisions under Article 6 and Article 8.
- 7.2 Board of directors of the Group Companies is entitled to nominate and appoint management staff and senior officers of the Group Companies, including but not limited to any legal representative of Chinese Subsidiary Company within the Group.





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#### Article 8 Sustaining Obligation

- 8.1 The Board of Directors shall be responsible for deciding and implementing all the Company policies. The Shareholders shall exercise all of their voting right and other rights in relation to the Company, and shall cause voting by directors appointed by them, as well as cause exercising respective rights of such directors to fully implement terms and conditions herein.
- 8.2 Subject to governing laws, the Parties shall modify the outline and bylaws of the Articles of Association to include all terms and conditions herein. In case of any inconsistency between the Agreement and the outline/bylaws of the Articles of Association, the Parties shall take necessary measures to modify the Articles of Association to eliminate such inconsistency.

#### Article 9 Restriction on Equity Transfer

- 9.1 Transfer Restrictions
- 9.1.1 Except for circumstances permitted under Article 9.2, Article 9.3, Article 9.4 and Article 11 as well as respective shares in the Company permitted to transfer to its affiliates by Heroic Vision and Kunlun, and without prior written consent of other Shareholders, any and all Shareholders may not:
- (a) Set encumbrance, via mortgage (regardless of fixed or floating pledge), pledge or other methods, to all or any part of the shares and/or legal or beneficially owned equity interest held by any Group Companies;
  - (b) Sell, transfer or dispose of, in any other ways, any shares and/or any legal or beneficially owned equity interest specified herein held by any Group Companies, or transfer or dispose of any interest included in the Agreement;
  - (c) Execute any agreement with which voting right of all or part of the shares and/or equity held by Group Companies is attached;
  - (d) Set any option, right, interest or encumbrance to any shares and/or equity of Group Companies; or
  - (e) Consent to the following events, regardless of conditions.
- 9.2 Pre-emptive Right
- 9.2.1 The Parties agree that, after the Closing Date, they may not issue shares to any other persons after the Company's capital increase, unless (1) approved by Shareholders in accordance with Article 5.1.1 and (2) subject to the requirements under Article 9.2 hereof. Heroic Vision and Kunlun are entitled to pre-emptive right towards shares issued due to capital increase ("Capital Increase Shares") based on their subscription ratio in accordance with the following formula.

$$\text{Subscription Ratio of Capital Increase Shares} = \frac{\text{Shares held by Heroic Vision or Kunlun (as the case may be)}}{\text{Total shares held by Heroic Vision and Kunlun}}$$



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- 9.2.2 The Parties agree that if the Board of Directors considers increasing issued shares is necessary for the need of Company Business, then notice ("Capital Increase Notice") shall be issued to Heroic Vision and Kunlun, and such notice shall specify:
- (a) Number of Capital Increase Shares;
  - (b) Subscription price for Capital Increase Shares; and
  - (c) Shares that may be subscribed by Heroic Vision and Kunlun in accordance with Article 9.2.1.
- 9.2.3 Heroic Vision and Kunlun shall issue notice on subscribing capital increase ("Notice on Subscription of Increased Capital") in thirty (30) days after receiving Capital Increase Notice, and the Notice on Subscription of Increased Capital shall specify the number of shares Heroic Vision and Kunlun, respectively, intends to subscribe at the subscription price listed on Capital Increase Notice. Heroic Vision and/or Kunlun shall give Notice on Subscription of Increased Capital to the Company and shall make a copy to the other Party. If Heroic Vision and/or Kunlun fail to give Notice on Subscription of Increased Capital in thirty (30) days upon receiving Capital Increase Notice, it shall be considered as having waived its pre-emptive right. If either of Heroic Vision and Kunlun fails to subscribe the full amount of shares as prescribed under Article 9.2.1, the other Party may subscribe the remaining shares via issuing Notice on Supplementary Subscription of Increased Capital ("Supplementary Notice on Subscription of Increased Capital") in ten (10) days upon receiving the Party's Notice on Subscription of Increased Capital. If Heroic Vision and/or Kunlun fail to give Notice on Supplementary Subscription of Increased Capital in ten (10) days upon receiving the other Party's Notice on Subscription of Increased Capital, it shall be considered as having waived its right of supplementary subscription.
- 9.2.4 Subject to the pre-emptive right of Heroic Vision and Kunlun, other Shareholders also have the pre-emptive right to subscribe the increased capital. After five (5) days upon receiving the Notice on Subscription of Increased Capital (and Notice on Supplementary Subscription of Increased Capital) issued by Heroic Vision and Kunlun or upon waiving pre-emptive right and the right of supplementary subscription in accordance with Article 9.2.3, the Company shall give notice to other Shareholders ("Notice of the Remaining Increased Capital for Subscription"), informing about the waived shares and subscription price in the increased capital. The other Shareholders may inform the Company about intention to subscribe certain shares in ten (10) days upon receiving Notice of the Remaining Increased Capital for Subscription. If any such Shareholder fails to inform the Company about its decision in ten (10) days, it shall be considered as having waived the pre-emptive right towards the remaining increased capital.
- 9.2.5 Upon expiration of the ten (10) -day-period as specified in the above Article 9.2.4, the Company shall have one hundred and twenty (120) days for it to sell the shares which are intended to issue to other persons on the same favorable terms and conditions as those having been given to the Shareholders. If the Company fails to make such issuance in one hundred and twenty (120) days, the Company must obtain approval based on Article 9.2 for another time if the Company intends to issue the shares.
- 9.3 Right of First Refusal
- 9.3.1 Under the same conditions, Heroic Vision or its affiliates shall enjoy the right of first refusal towards any shares ("Shares Transferred") that Kunlun intends to transfer to any person ("Transferee").
- 9.3.2 Before Kunlun's transfer of any shares, Kunlun shall give written notice ("Transfer Notice") to Heroic Vision, specifying (a) number of shares to be transferred; (b) conditions for such transfer (referred to as "Transfer Conditions", including transfer price and other conditions); (c) identity of the transferee; (d) such notice may not be withdrawn or cancelled.



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- 9.3.3 Heroic Vision shall give written notice (“Receiving Notice”) to Kunlun in thirty (30) days upon receiving Transfer Notice as described in Article 9.3.2, specifying that Heroic Vision or its affiliate intends to purchase the Shares Transferred in accordance with Transfer Conditions. If Heroic Vision fails to give Receiving Notice to Kunlun in thirty (30) days upon receiving Transfer Notice, it shall be considered as having waived its right of first refusal unless otherwise approved by Kunlun.
- 9.3.4 Kunlun agrees that Heroic Vision shall not transfer any Shares Transferred to Kunlun preceding its exercising or waiving the right of first refusal in accordance with Article 9.3.
- 9.3.5 Upon expiration of the thirty (30) -day-period as specified in the above Article 9.3.2, Kunlun shall have one hundred and twenty (120) days for it to sell the shares not purchased by Heroic Vision which are intended to issue to the transferee on the same favorable terms and conditions as those having been given to the Heroic Vision. If Kunlun fails to make such transfer in one hundred and twenty (120) days, the Company must obtain approval based on Article 9.3 for another time if the Company intends to transfer the shares.
- 9.4 Deed of Adherence
- Regardless of provisions in other terms and conditions herein, any Shareholder and the Company may not transfer the shares in the Company it holds, unless:
- (a) For Management Shareholders, the Management Shareholder, receiving equity, accepts the restrictions of the terms and conditions applicable in the Agreement in the written form of Management Shareholder’s Deed of Adherence, whose content shall be consistent with Annex 2 hereof;
  - (b) For transferees other than the Management Shareholders, such transferee accepts the restrictions of the terms and conditions applicable in the Agreement in the written form of Transferee’s Deed of Adherence, whose content shall be consistent with Annex 3 hereof;
  - (c) The transfer meets other applicable terms and conditions herein in all respects;
  - (d) The transfer meets the governing laws in all respects; and
  - (e) The transferor, with respect to the Shares Transferred, does not enjoy any rights or assume any obligations hereunder or under any other transactions documents.

#### **Article 10 Performance Guarantee and Shares Adjustment**

- 10.1 The Parties agree that the Investment Agreement executed by Heroic Vision is based on the following expected performance (“2014 Annual Goal”) of the Group.
- 10.1.1 Kunlun guarantees that \* (\*) of RaidCall voice service (www.raidcall.com) outside China during December, 2014 will not be below \*.
- 10.1.2 In case of any abnormal or improper means (such as self-consuming, artificial control of the flow, interfering with flow system, etc.) that manipulate or influence the \* of RC voice service (www.raidcall.com), resulting in the achievement of 2014 Annual Goal, then it shall be considered as not achieved.

**The symbol ‘ \* ’ in this exhibit indicates places where information has been omitted pursuant to a request for confidential treatment and filed separately with the SEC.**



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- 10.2 If the Group fails to achieve the 2014 Annual Goal, Kunlun, Management Shareholders and the Company shall together transfer the Company's shares, free of charge, calculated via the following formula (Kunlun shall undertake 60% of the adjusted shares; Management Shareholders shall undertake 40% of the adjusted shares, and if the shares held by the Management Shareholders are not sufficient, the remaining part shall be undertaken by the Company via Treasury Shares):
- Adjusted shares = 70% X All issued shares in the Company (for avoidance of doubt, all Treasury Shares issued externally shall be included) – Shares held by Heroic Vision.
- 10.3 After Heroic Vision delivers reasonable document evidencing the non-achievement of 2014 Annual Goal to Kunlun, Heroic Vision may deliver the notice regarding its exercising rights under Article 10.2 ("Notice of Exercise") to Kunlun at any time.
- (a) Kunlun shall, in five (5) business days ("Period for Notice of Exercise") upon service of Notice of Exercise, transfer the determined shares (without any encumbrance) in accordance with Article 10.2 to Heroic Vision, through delivering share certificates displaying the number of shares intending to be transferred together with Transfer Document duly executed in effective form and in accordance with material requirements; or
- (b) In case of objection towards supporting documents submitted by Heroic Vision, written notice shall be sent to Heroic Vision within the Period for Notice of Exercise to carry out amicable negotiation. If consensus is not achieved in twenty (20) business days upon the first day of negotiation, Kunlun and Heroic Vision both are entitled to submit the dispute to HKIAC in accordance with Article 17.3 for arbitration. For avoidance of doubt, if Kunlun fails to propose objection during the Period for Notice of Exercise, then it shall be considered as Kunlun does not having objection against the recognition of 2014 Annual Goal, and shall perform the share transfer obligation in accordance with the Paragraph (a) of this Article.

#### **Article 11 Management Share Option Incentive Plan**

- 11.1 The Parties agree that the Company has set up Management Share Option Incentive Plan to grant options to the Company's management, making them receive the Company's shares when exercising such options ("Management Share Option Incentive Plan"). At Closing, the Company has 1,500 ordinary shares, representing 15% of the Company's shares (based on full dilution), as Treasury Shares, which shall be transferred to the Company's management as Share Option in accordance with Article 11.
- 11.2 The Parties agree that the Company's Board of Directors shall determine the procedures and content of the Management Share Option Incentive Plan, and the Board may participate in the management of such Management Share Option Incentive Plan as well as determination of the number of shares to be granted (including corresponding Share Option). The management shall obtain 25% of the granted exercising ability each year in the following four (4) years (i.e. obtaining 25%, 50%, 75% and 100% of the granted exercising ability on the first anniversary, second anniversary, third and the fourth anniversary of the granting day). If one of the management staff leaves his/her position in the four (4) years, then option of which exercise ability has not been granted shall be invalid, and the corresponding exercise ability may not be obtained since then. Subject to the provisions of Article 9.4, the management may perform the exercise ability toward options already granted, and receive Share Option from the Company without any payment.



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#### Article 12 Return from Preferred Liquidation

- 12.1 Subject to governing laws, if the Company endures termination, cancellation, dissolution or any other events resulting in liquidation, the Company shall allocate the remaining assets to Shareholders based on shareholding ratio after paying all liquidation fees and liabilities in accordance with the governing law.
- 12.2 If the value of the remaining assets of the Company, received by Heroic Vision in accordance with Article 12.1, is less than the amount of return liquidation priority, then Kunlun and Management Shareholders (if applicable) agree and hereby transfer part or all of the assets allocated through liquidation entitled to Heroic Vision upon termination or dissolution of the Company, in order to make Heroic Vision have the assets whose value is equivalent to 65,000,000 USD ("Amount of Return from Preferred Liquidation") upon the Company's termination or dissolution. Heroic Vision hereby agrees to such transfer.

#### Article 13 Non-competition and Non-solicitation

13.1 Kunlun and Management Shareholders hereby undertake to Heroic Vision and the Company that:

- (a) As of the Closing Date in respect of Kunlun;
- (b) As of the acquisition of shares in the Company pursuant to Article 11 in respect of Management Shareholders, they shall not and shall ensure their affiliates (excluding each Group Company) and key personnel may not directly or indirectly, solely or jointly with other Parties engage in, or directly or indirectly, solely or jointly with other Parties through establish any other commercial entity engage in any businesses or activities which are as the same as or similar with that of the group, including research, development, marketing, promotion, service render or license grant ("Restricted Business") or hold any interest in such business or activities.

13.2 Kunlun and Management Shareholders hereby undertake to Heroic Vision and the Company that:

- (a) As of the Closing Date in respect of Kunlun;
- (b) As of the acquisition of shares in the Company pursuant to Article 11 in respect of Management Shareholders, they shall not and shall ensure all of their affiliates (excluding each Group Company) may not hire any employee or former employee of each Group Company, Heroic Vision or any affiliates of Heroic Vision in any way (whether directly or indirectly) or solicit any of such person to engage in Restricted Business.

13.3 If any part of this Article has become invalid, illegal or unenforceable in any aspect for any reason, such invalid, illegal or unenforceable provision shall not affect the effect of the other part in this Article and this Article shall be interpreted as if such invalid, illegal or unenforceable provision has never been contained herein. Article 17.8 shall be applied to such case. Kunlun and Management Shareholders confirm that Heroic Vision and the Company may incur irreparable damage for any of its breach of this Article and no relief for indemnification may be adequate for the loss of Heroic Vision and/or the Company incurred for such breach. Kunlun and Management Shareholders agree that Heroic Vision and the Company shall be entitled to exercise the injunctive relief to require the actual performance of the Article 13 by Kunlun and Management Shareholders and Kunlun and Management Shareholders shall agree with the exercise of such right.

13.4 For the avoidance of doubt, any breach of any provisions in this Article by any affiliate (excluding each Group Company) of Kunlun and/or Management Shareholders shall be deemed as the breach of Kunlun and/or Management Shareholders.



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- 13.5 In case of any breach of this Article 13 of Kunlun and/or Management Shareholders, it shall be deemed as materially breaching the Agreement and Heroic Vision and the Company shall be entitled to require the payment of liquidated damage by Kunlun or Management Shareholders. The specific amount of such liquidated damage shall be subject to the higher of USD 2million or total loss incurred by Heroic Vision. Such amount shall be paid by Kunlun or Management Shareholders to the bank account designated by Heroic Vision and the Company as soon as possible, but in no event shall be later than ten (10) business days after it receives the notice from Heroic Vision and/or the Company requiring such payment. The Parties confirm and agree that such amount shall be real estimation on the loss relevant breach may cause and shall be the supplementary to any other rights or remedies which may be obtained by Heroic Vision and the Company pursuant to laws or contracts and shall not substitute or reduce any such other rights or remedies.

#### Article 14 Presentation and Warranty

The Parties solely, rather than jointly, hereby make the following presentations and warranties to other Parties and undertake that:

##### 14.1 Incorporation, Good Standing and Qualifications

The Parties (1) are limited companies legally organized in accordance with the applicable law in the places of their respective incorporation and valid existing and with good standing and have obtained the consents of all relevant governmental authorities for its incorporation (if necessary); (2) have all powers and authorizations necessary for the possession and operation of its property and the conduction of its business and for the execution, delivery and performance hereof as well as for the completion of the transactions proposed hereunder; (3) have proper qualifications to conduct its business and transactions and the licenses and qualifications necessary for the operation of such business and have the good standing in each jurisdiction in which such qualification are required; and (4) operate its business in compliance with applicable laws at all times since its incorporation.

##### 14.2 Authorization

- 14.2.1 The Parties have taken all necessary actions to authorize, execute and deliver the Agreement and to perform their respective obligations hereunder. The Agreement shall constitute a valid obligation and legally binding upon them and may be performed pursuant to the terms hereunder.

- 14.2.2 The execution, delivery or performance hereof or the completion of the transaction proposed hereunder by the Parties needs no additional consent from any person except the consent obtained on the Closing Date.

##### 14.3 No Breach

The execution, delivery or performance hereof or the completion of the transaction proposed hereunder by the Parties shall not (i) constitute a conflict with any applicable law; (ii) constitute a breach of any provisions of any contract or result in any right to any termination or cancellation or early termination or cancellation of any rights or obligation of any Party under any provision in any contract, or result in the loss of any interest of any Party under any provision in any contract or any increase of the interest rate currently effective for any liability of each Party; or (iii) result in any encumbrance to any property or asset of each Party (except the encumbrance expressly consented by the Parties in transaction documents).

##### 14.4 Insolvency

The Parties will not and have no reason to believe that they will suffer an insolvency or unable to pay the matured debt in a foreseeable future pursuant to applicable laws. There is no and they have no reason to believe that there will be any compromise with creditors or no related legal procedure or procedure related to the liquidation, bankruptcy or other dismission procedures will be arranged and as to the knowledge of the Parties, there is no event which may trigger such legal procedures.



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#### Article 15 Termination

##### 15.1 Term and Termination of the Agreement

The Agreement shall come into effect as of the Closing Date and shall remain in effect until and unless be terminated in the following circumstances:

##### 15.1.1 The Parties mutually agree to terminate the Agreement in advance;

##### 15.1.2 Company Dissolution;

##### 15.1.3 As to each Shareholder, all of its shares are sold.

##### 15.2 Effectiveness of the Termination

Except the case provided in Article 15.3, the Agreement shall be invalid if it is terminated in accordance with the provisions specified in Article 15.1 or with applicable laws, provided, however, that the Parties shall not be exempted from the liabilities arising from or caused by the breach or any misrepresentation of it hereunder and such termination shall not be deemed as the waiver of any receivable remedy for any such breach or misrepresentation, including actual performance, if receivable.

##### 15.3 Remain in Effect

The provisions specified in Article 15, 16 and 17 shall remain in effect after the termination hereof.

#### Article 16 Confidentiality

##### 16.1 Confidentiality Obligation

Each Party hereof shall strictly keep the information contained herein or acquired or obtained due to the negotiation and/or execution hereof in confidence and shall not disclose or use such information, including any information related to the following items:

##### 16.1.1 The existence of the Agreement and the provisions hereof;

##### 16.1.2 Negotiation related to the Agreement; or

##### 16.1.3 Business activity of any Party hereof, of such Party or of any of their affiliates.

##### 16.2 Permitted Disclosure

Provided, however, that in the following cases, Article 16.1 shall not be applied to the disclosure or use of any information to the following extent:

##### 16.2.1 Disclosure or use required by applicable laws, by any rules of the stock exchange where share of any Party listed in or by any governmental authority, provided that related Party shall inform other parties about such requirement prior to the disclosure or the use to provide other parties with an opportunity to refuse such disclosure or use or to discuss the time and content thereof;

##### 16.2.2 Disclosure or use necessary for the purpose of any legal procedure arising from the Agreement or from any other agreements executed hereunder or pursuant hereto, or the disclosure is made to any tax authority due to tax affairs related to the disclosing party;

##### 16.2.3 Disclosure made to the representative of any Party who requires learning such information for the purpose of completing transactions hereunder or under other agreements concluded pursuant hereto, provided that such representative undertakes to comply with Article 16.1 in respect of such information, as if it is a party hereof;





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- 16.2.4 Such information may be acquired from public domain [except such information may be acquired as a result of breaching the Confidentiality Agreement (if any) or the Agreement]; or
- 16.2.5 Written consents have been made by other parties prior to the disclosure or use.

#### Article 17 General Provisions

- 17.1 Binding; Transfer
- The Agreement shall be binding upon the Parties, their respective successor and permitted transferee and shall be enforceable. The Parties may not transfer any of their rights or obligations hereunder without the prior written approval of other parties; however, Heroic Vision and Kunlun shall be entitled to transfer all or part of their respective rights and obligations hereunder to any of their respective affiliates without the prior consent of other parties.
- 17.2 Governing Law
- The Agreement shall be governed by and interpreted in accordance with laws of Hong Kong.
- 17.3 Dispute Settlement
- 17.3.1 Any dispute, argument or claim arising from or related to the Agreement or the interpretation, breach, termination or validity hereof (each a "Dispute") shall be firstly settled by the disputing parties through negotiation. The negotiation shall be started upon the delivery of a written notice by any Party to any other parties requiring so.
- 17.3.2 If the Dispute fails to be settled within sixty (60) days after the delivery of such notice, the Dispute shall be submitted for arbitration upon the delivery of a written notice by any disputing party to any other parties requiring so (hereinafter referred to as "Arbitration Notice").
- 17.3.3 The Dispute shall be submitted to Hong Kong International Arbitration Center ("HKIAC") and be arbitrated in Hong Kong. The arbitration shall be made by three (3) arbitrators who shall be appointed pursuant to the arbitration rules of HKIAC ("Arbitration Rules") in effect at the arbitration unless otherwise expressly provided in this Article 17.3.3. One arbitrator shall be appointed by Heroic Vision; the second arbitrator shall be appointed jointly by Heroic Vision and Kunlun within ten (10) days after the appointment of Heroic Vision in case of Kunlun is involved in all such arbitrations; otherwise, the second arbitrator shall be appointed by HKIAC; the third arbitrator shall be the chief arbitrator and jointly appointed by arbitrators within ten (10) days after the date of the later arbitrator is appointed; otherwise, such third arbitrator shall be appointed by HKIAC.
- 17.3.4 The arbitration shall be made in Chinese. The arbitration court shall apply the Arbitration Rules.
- 17.3.5 The arbitration award made by the arbitration court shall be final and binding upon the Parties; the winning party may apply the execution of such award with the court with jurisdiction.
- 17.3.6 Any Party involved in the Dispute shall be entitled to seek temporary injunctive relief in any court with jurisdiction, where practicable.
- 17.3.7 The Agreement shall be continuously performed during the arbitration course except the part to be arbitrated.



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- 17.3.8 The arbitration fee shall be undertaken by the losing party in the arbitration pursuant to the arbitration award, including legal fee, accountant fee and costs and expenses for other professionals arising from the survey, collection, prosecution and/or defense made by any winning party for any request in dispute.
- 17.4 Amendment
- Unless otherwise permitted herein, any amendment, change, waiver, cancellation or termination hereof or of any provisions herein shall be made in written documents signed by each Party.
- 17.5 Notice
- 17.5.1 All notices, claims for rights, certifications, requests, requirements and other communications given to any other Party hereunder shall be made in writing and shall be delivered to such Party by person, facsimile or overnight courier service of good faith with a prepaid postage at the address listed in Article 17.5.2 or at any other addresses pointed by such Party in a notice to other parties. Such communications shall be deemed as delivered (i) at its delivery if by hand; (ii) upon receiving the receipt if by facsimile; and (iii) within five (5) calendar days after being delivered to or received by the courier.
- 17.5.2 The notices hereunder shall be delivered to the Parties at following addresses and received by the following person:
- Kunlun: Koram Games Limited
- Address: Suite 5118, 51th Floor, Hopewell Centre, No. 183 Queen's Road East, Wanchai, Hong Kong
- Fax: 00852-36023071
- Recipient: Zhou Yahui
- HEROIC VISION: HEROIC VISION HOLDINGS LIMITED
- Address: Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing
- Fax: 86-10-68874008
- Recipient: Legal Department of Heroic Vision
- Company: TalkTalk Limited
- Prior to the Closing Date
- Address: Tower B, Mingyang International Center, No. 46, Xizongbu Alley, Dongcheng District, Beijing
- Fax: 86-10-65210297
- Recipient: Zhou Yahui



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After the Closing Date

Address: Floor 2, East Tower, Jingyan Hotel, No. 29 Shijingshan Road, Shijingshan District, Beijing

Fax: 86-10-68874008

Recipient: Legal Department of Heroic Vision

17.6 Further Warranty

Each Party shall make and perform (or cause other party to make and perform) all further actions and matters and shall execute and deliver all other agreements, certificates, instruments and documents, which may be reasonably required by any other parties for the achievement of the provisions and the purpose hereof.

17.7 Entire Agreement

The Agreement and all other transaction documents shall jointly constitute the entire agreement among the Parties in respect of the subject hereof and supersede all previous written or oral understandings or agreements.

17.8 Severability

If any provisions hereof are deemed as void or unenforceable to some extent, the remaining provisions shall not be affected and shall be performed to the maximum extent permitted by law. Any invalid or unenforceable provisions of the Agreement shall be replaced by other valid and enforceable provisions, and such provisions shall have the proximal effectiveness with the original meaning of unenforceable provisions herein.

17.9 Cumulative Remedies

All rights and remedies provided herein or obtained in other ways shall be accumulated and exercised in succession with all other rights and remedies.

17.10 Counterparts

The Agreement may be executed in one or more counterparts, each of which shall be deemed as an original but all of which shall constitute one and the same document.



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IN WITNESS WHEREOF, the Parties hereof have caused their respective authorized representatives to execute the Agreement as of the date first written above.

Koram Games Limited

Signatory: /s/ Zhou Yahui

Name: Zhou Yahui

HEROIC VISION HOLDINGS LIMITED

Signatory: /s/ Wang Tao

Name: Wang Tao

TalkTalk Limited

Signature: /s/ Zhou Yahui

Name: Zhou Yahui



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### Annex I Definitions

<b>“2014 Annual Goal”</b>	Shall have the meaning set forth in Article 10.1.
<b>“The Agreement”</b>	Shall have the meaning set forth in the Recitals hereof.
<b>“Notice on Supplementary Subscription of Increased Capital”</b>	Shall have the meaning set forth in Article 9.2.3.
<b>“Heroic Vision”</b>	Shall have the meaning set forth in the Recitals hereof.
<b>“Subsidiary Company”</b>	Means the subsidiary company established anywhere by the person who: (1) is in charge of the board of directors of such subsidiary company; (2) controls over 50% of its voting rights; (3) holds over 50% of its issued shares (excluding those shares for which such person has no right to include in the profit or capital distribution exceeding the specified amount); or (4) owns one subsidiary company of such company.
<b>“Parties” or “Party”</b>	Shall have the meaning set forth in the Recitals hereof.
<b>“Company”</b>	Shall have the meaning set forth in the Recitals hereof.
<b>“Shareholder”</b>	Means the holder of the Company’s shares.
<b>“Management Shareholders”</b>	Means the employees in management who are determined by Xiang Gensheng, Hu Bin and the Shareholders’ Meeting from time to time.
<b>“Management Share Option Incentive Plan”</b>	Shall have the meaning set forth in Article 11.1.
<b>“Meeting Notice”</b>	Shall have the meaning set forth in Article 5.2.
<b>“Group”</b>	Means the Company and its affiliates from time to time; Group Company means any company of them.
<b>“Group Business”</b>	Means RaidCall voice service and other related businesses.
<b>“Closing Date”</b>	Means the date on which the closing is made pursuant to the Investment Agreement.
<b>“Kunlun”</b>	Shall have the meaning set forth in the Recitals hereof.
<b>“*(*)”</b>	Means *.
<b>“Share Option”</b>	Means Company shares which may be acquired after the exercise of the option in Management Share Option Incentive Plan.

The symbol “\*” in this exhibit indicates places where information has been omitted pursuant to a request for confidentially treatment and filed separately with the SEC.



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<b>“Notice on Subscription of Increased Capital”</b>	Shall have the meaning set forth in Article 9.2.3.
<b>“Transferee”</b>	Shall have the meaning set forth in Article 9.3.1.
<b>“Receiving Notice”</b>	Shall have the meaning set forth in Article 9.3.3.
<b>“Notice of the Remaining Increased Capital for Subscription”</b>	Shall have the meaning set forth in Article 9.2.4.
<b>“Investment Agreement”</b>	Means the investment agreement concluded by Heroic Vision, Kunlun, Beijing Kunlun Technology Co., Ltd., Guangzhou Kunlun Online Information Technology Co., Ltd. and Kunlun Korea Co., LTD. on November 19, 2013.
<b>“Restricted Business”</b>	Shall have the meaning set forth in Article 13.1.
<b>“Notice of Exercise”</b>	Shall have the meaning set forth in Article 10.3.
<b>“Period for Notice of Exercise”</b>	Shall have the meaning set forth in Article 10.3.
<b>“Amount of Return from Preferred Liquidation”</b>	Shall have the meaning set forth in Article 12.2.
<b>“Capital Increase Share”</b>	Shall have the meaning set forth in Article 9.2.1.
<b>“Capital Increase Notice”</b>	Shall have the meaning set forth in Article 9.2.2.
<b>“Dispute”</b>	Shall have the meaning set forth in Article 17.3.1.
<b>“Arbitration Rules”</b>	Shall have the meaning set forth in Article 17.3.3.
<b>“Arbitration Notice”</b>	Shall have the meaning set forth in Article 17.3.2.
<b>“Shares Transferred”</b>	Shall have the meaning set forth in Article 9.3.1.
<b>“Transfer Conditions”</b>	Shall have the meaning set forth in Article 9.3.2.
<b>“Transfer Notice”</b>	Shall have the meaning set forth in Article 9.3.2.



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## Annex II Deed of Adherence of Management Shareholders

This Deed of Adherence (“Deed”) is concluded and executed on [Date] by:

- (1) Koram Games Limited, a limited company established and existing in accordance with laws of Hong Kong (registration number: 1415564) with its registered office at Suite 1203, 12<sup>th</sup> Floor, Ruttonjee House, 11 Duddell Street, Central, Hong Kong (“Kunlun”);
  - (2) HEROIC VISION HOLDINGS LIMITED, a limited company established and existing in accordance with laws of British Virgin Islands (registration number: 1795916) with its registered office at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (“Heroic Vision”); and
  - (3) TalkTalk Limited, a limited company established and existing in accordance with laws of British Virgin Islands (registration number: 1799119) with its registered office at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (“Company”);
- (Kunlun, Heroic Vision and the Company are called collectively as the “Existing Shareholders”)
- (4) [●], holder of the Chinese ID card No. [●] who lives in [●] (“New Shareholder”).

Whereas:

- A. The Existing Shareholders have concluded a shareholder agreement (“Shareholder Agreement”) on [●] to prescribe the relationship among the Existing Shareholders as the Company’s shareholder and the terms of the agreement concluded by them in respect of the operation and management of the Company. A counterpart of Shareholder Agreement has been attached hereof and is remarked as “A” for the convenience of identification.
- B. The Company has agreed to, pursuant to the [●] concluded by the New Shareholder and it (“Transfer Document”), transfer the ownership of the legal and beneficial interests in its [●] common shares to the New Shareholder (“Transferred Interest”) on [●].
- C. Each party hereof shall conduct the closing upon the execution of the Deed (“Closing”) so that the New Shareholder can act as the owner and holder of the beneficial and legal interest in the Transferred Interest.
- D. The Deed shall be the supplementary agreement of the Shareholder Agreement.

Following agreements have been made through negotiation:

1. Unless otherwise defined herein, the terms and expressions used herein shall share the same definition with that defined in the Shareholder Agreement.
2. The New Shareholder confirms that it has read the Shareholder Agreement and hereby undertakes to the Existing Shareholders that it will act as a Management Shareholder to fully perform, undertake and comply with all terms, undertakings, obligations and provisions under the Shareholder Agreement as of the Closing as if it is an original party of the Shareholder Agreement and holds the Transferred Interest in related periods.





**Confidential Treatment Requested. Confidential portions of this document have been redacted and have been separately filed with the SEC.**

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3. For the purpose set forth in Article 17.5.2 of the Shareholder Agreement, the New Shareholder shall be notified in the following way:

New Shareholder:

Address:

Fax:

Recipient:

4. Unless otherwise changed or supplemented, the Shareholder Agreement shall be in full valid and effect.
5. The Deed shall be governed by laws of Hong Kong and all disputes, arguments or claims arising from or related hereto or any breach, termination or invalid resulting therefrom shall be settled in a way provided in the Shareholder Agreement.
6. As of the effective date of the Deed, the Deed and the Shareholder Agreement shall constitute one document, provided, however, that the provisions herein shall prevail in case of any conflict between the Deed and the Shareholder Agreement.

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**Confidential Treatment Requested. Confidential portions of this document have been redacted and have been separately filed with the SEC.**

IN WITNESS WHEREOF, the deed has been delivered as of the date first written above.

Executed )  
and delivered as a deed by )  
Koram Games Limited )  
in the presence of )

Executed )  
and delivered as a deed by )  
HEROIC VISION HOLDINGS LIMITED )

in the presence of

Executed )  
and delivered as a deed by )  
TalkTalk Limited )  
in the presence of )

Executed )  
and delivered as a deed by )  
[New Shareholder] )  
in the presence of )



**Confidential Treatment Requested. Confidential portions of this document have been redacted and have been separately filed with the SEC.**

### Annex III Deed of Adherence of Other Transferees

This Deed of Adherence is concluded and executed on [●] [●], 2013 by:

- (1) Koram Games Limited, a limited company established and existing in accordance with laws of Hong Kong (registration number: 1415564) with its registered office at Suite 1203, 12<sup>th</sup> Floor, Ruttonjee House, 11 Duddell Street, Central, Hong Kong (“Kunlun”);
  - (2) HEROIC VISION HOLDINGS LIMITED, a limited company established and existing in accordance with laws of British Virgin Islands (registration number: 1795916) with its registered office at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (Heroic Vision); and
  - (3) TalkTalk Limited, a limited company established and existing in accordance with laws of British Virgin Islands (registration number: 1799119) with its registered office at P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands (“Company”);
- (Kunlun, Heroic Vision and the Company are called collectively as the “Existing Shareholders”)
- (4) [●], [a limited company established and exists in accordance with [●] (Registration No.: [●])/ holder of the Chinese ID card No. [●]], [with its registered office at [●]/lives in [●]] (“New Shareholder”).

Whereas:

- A. The Existing Shareholders have concluded a shareholder agreement (“Shareholder Agreement”) on [●] to prescribe the relationship among the Existing Shareholders as the Company’s shareholder and the terms of the agreement concluded by them in respect of the operation and management of the Company. A counterpart of Shareholder Agreement has been attached hereof and is remarked as “A” for the convenience of identification.
- B. [Name of the Transferor] has agreed to, pursuant to the [●] concluded by the New Shareholder and it (“Transfer Document”), transfer the ownership of the legal and beneficial interests in its [●] common shares to the New Shareholder (“Transferred Interest”) on [●].
- C. Each party hereof shall conduct the closing upon the execution of the Deed so that the New Shareholder can act as the owner and holder of the beneficial and legal interest in the Transferred Interest.
- D. The Deed shall be the supplementary agreement of the Shareholder Agreement.

Following agreements have been made through negotiation:

1. Unless otherwise defined herein, the terms and expressions used herein shall share the same definition with that defined in the Shareholder Agreement.
2. The New Shareholder confirms that it has read the Shareholder Agreement and hereby undertakes to the Existing Shareholders that it will act as a Transferor to fully perform, undertake and comply with all terms, undertakings, obligations and provisions under the Shareholder Agreement as of the Closing as if it is an original party of the Shareholder Agreement and holds the Transferred Interest in related periods.



**Confidential Treatment Requested. Confidential portions of this document have been redacted and have been separately filed with the SEC.**

---

3. For the purpose set forth in Article 17.5.2 of the Shareholder Agreement, the New Shareholder shall be notified in the following way:

New Shareholder:

Address:

Fax:

Recipient:

4. Unless otherwise changed or supplemented, the Shareholder Agreement shall be in full valid and effect.
5. The Deed shall be governed by laws of Hong Kong and all disputes, arguments or claims arising from or related hereto or any breach, termination or invalid resulting therefrom shall be settled in a way provided in the Shareholder Agreement.
6. As of the effective date of the Deed, the Deed and the Shareholder Agreement shall constitute one document, provided, however, that the provisions herein shall prevail in case of any conflict between the Deed and the Shareholder Agreement.

[THE REMAINDER OF THIS PAGE IS INTENTIONALLY LEFT BLANK]



**Confidential Treatment Requested. Confidential portions of this document have been redacted and have been separately filed with the SEC.**

IN WITNESS WHEREOF, the deed has been delivered as of the date first written above.

Executed )  
and delivered as a deed by )  
Koram Games Limited )  
in the presence of )

Executed )  
and delivered as a deed by )  
HEROIC VISION HOLDINGS LIMITED )  
in the presence of )

Executed )  
and delivered as a deed by )  
TalkTalk Limited )  
in the presence of )

Executed )  
and delivered as a deed by )  
[New Shareholder] )  
in the presence of )





## Exhibit 8.1

### List of Subsidiaries of the Registrant

- Changyou.com (HK) Limited, incorporated in Hong Kong.
- ICE Entertainment (HK) Limited, incorporated in Hong Kong.
- Beijing AmazGame Age Internet Technology Co., Ltd., incorporated in the PRC.
- Beijing Changyou Gamespace Software Technology Co., Ltd., incorporated in the PRC.
- ICE Information Technology (Shanghai) Co., Ltd., incorporated in the PRC.
- Beijing Yang Fan Jing He Information Consulting Co., Ltd., incorporated in the PRC.
- Shanghai Jingmao Culture Communication Co., Ltd., incorporated in the PRC.
- Beijing Changyou Jingmao Film & Culture Communication Co., Ltd., incorporated in the PRC.
- Shanghai Hejin Data Consulting Co., Ltd., incorporated in the PRC.
- Changyou.com (US) LLC, formed in the United States.
- Changyou.com (UK) Co., Ltd., incorporated in the United Kingdom.
- Changyou My Sdn. Bhd, incorporated in Malaysia.
- Changyou.com Korea Limited, incorporated in South Korea.
- Changyou.com India Private Limited, incorporated in India.
- Changyou.com Gamepower (HK) Limited, incorporated in Hong Kong.
- Changyou.com Webgames (HK) Limited, incorporated in Hong Kong.
- 7Road.com Limited, incorporated in the Cayman Islands.
- 7Road.com HK Limited, incorporated in Hong Kong.
- Shenzhen 7Road Network Technologies Co., Ltd., incorporated in the PRC.
- CHANGYOU BİLİŞİM HİZMETLERİ TİCARET LİMİTED ŞİRKETİ, incorporated in Turkey.
- Kylie Enterprises Limited, incorporated in British Virgin Islands.
- Changyou.com Gamestar (HK) Limited, incorporated in Hong Kong.
- Heroic Vision Holdings Limited, incorporated in British Virgin Islands.
- Mobogarden Enterprises Limited, incorporated in British Virgin Islands.

As of the date of this annual report, we also own, through Heroic Vision Holdings Limited, the following subsidiaries:

- TalkTalk Limited, incorporated in British Virgin Islands.
- RaidCall (HK) Limited, incorporated in Hong Kong.
- Beijing Changyou RaidCall Internet Technology Co., Ltd., incorporated in the PRC.



# Exhibit 12.1

I, Tao Wang, certify that:

1. I have reviewed this annual report on Form 20-F of Changyou.com Limited;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls over financial reporting.

Date: February 28, 2014

By: /s/ Tao Wang  
 Name: Tao Wang  
 Title: Chief Executive Officer



**Exhibit 12.2**

I, Alex Ho, certify that:

1. I have reviewed this annual report on Form 20-F of Changyou.com Limited;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls over financial reporting.

Date: February 28, 2014

By: /s/ Alex Ho  
 Name: Alex Ho  
 Title: Chief Financial Officer



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CHANGYOU.COM LIMITED

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**Exhibit 13.1**CERTIFICATIONPURSUANT TO RULE 13A-14(B) UNDER THE SECURITIES EXCHANGE ACT OF 1934

In connection with the Annual Report on Form 20-F of Changyou.com Limited (the "Company") for the year ended December 31, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Tao Wang, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition of the Company as of December 31, 2013 and results of operations of the Company for the year ended December 31, 2013.

/s/ Tao Wang

Name: Tao Wang

Title: Chief Executive Officer

Date: February 28, 2014



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**CHANGYOU.COM LIMITED**  
**FORM 20-F**

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**Exhibit 13.2****CERTIFICATION****PURSUANT TO RULE 13A-14(B) UNDER THE SECURITIES EXCHANGE ACT OF 1934**

In connection with the Annual Report on Form 20-F of Changyou.com Limited (the "Company") for the year ended December 31, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Alex Ho, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition of the Company as of December 31, 2013 and results of operations of the Company for the year ended December 31, 2013.

/s/ Alex Ho

Name: Alex Ho

Title: Chief Financial Officer

Date: February 28, 2014



**Exhibit 15.1**

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8 (No. 333-161727) of Changyou.com Limited of our report dated February 28, 2014 relating to the consolidated financial statements and the effectiveness of internal control over financial reporting, which appears in this Form 20-F.

/s/ PricewaterhouseCoopers Zhong Tian LLP

PricewaterhouseCoopers Zhong Tian LLP  
Beijing, the People's Republic of China  
February 28, 2014



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**CHANGYOU.COM LIMITED**

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**Exhibit 15.2**

February 28, 2014

Changyou.com Ltd.  
East Tower, JingYan Building,  
No. 29 Shijingshan Road, Shijingshan District,  
Beijing 100043  
People's Republic of China

Subject: Consent of Haiwen & Partners

We hereby consent to the filing of this consent letter as an exhibit to the annual report on Form 20-F of Changyou.com Limited (the "Company") for the Company's fiscal year ended December 31, 2013, being filed with the U.S. Securities and Exchange Commission (the "SEC") on February 28, 2014 (the "Form 20 F").

We also hereby consent to the use of our firm name and summaries of our firm's opinions under the headings "Business Overview – PRC Regulation" and "Organizational Structure" in the Form 20-F and to the incorporation by reference in the Company's Registration Statement on Form S-8 (File No. 333-161727), initially filed with the SEC on September 4, 2009, of such references to our firm and summaries of our firm's opinions included under such headings.

Yours faithfully,

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**Haiwen & Partners**