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

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**FORM 20-F**

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(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 September 30, 2011

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**

Date of event requiring this shell company report

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-34122

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**China Distance Education Holdings Limited**

(Exact name of Registrant as specified in its charter)

Not applicable

(Translation of Registrant's name into English)

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Cayman Islands

(Jurisdiction of incorporation or organization)

18th Floor, Xueyuan International Tower  
1 Zhichun Road, Haidian District  
Beijing 100083, People's Republic of China  
(Address of principal executive offices)

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

Title of each class  
**American Depositary Shares, each representing four  
ordinary shares, par value \$0.0001 per share**

Name of each exchange on which registered  
**New York Stock Exchange, Inc.**

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**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**

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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: 127,800,673 ordinary shares

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

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

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

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

Except where the context otherwise requires and for purposes of this annual report only:

- all references to years are to the calendar year from January 1 to December 31 and references to our fiscal year or years are to the fiscal year or years ended September 30;
- “we,” “us,” “our company,” “our,” and “CDEL” refer to China Distance Education Holdings Limited and its subsidiaries and PRC affiliated entity, Beijing Champion Hi-Tech Co., Ltd., or Beijing Champion and its subsidiaries, as the context requires;
- “China,” “Chinese” and “PRC” refers to the People’s Republic of China, excluding, for purposes of this annual report only, Taiwan and the Special Administrative Regions of Hong Kong and Macau;
- all references to “Renminbi” or “RMB” are to the legal currency of China, and all references to “U.S. dollar,” “dollar,” “\$” or “US\$” are to the legal currency of the United States;
- “U.S. GAAP” refers to generally accepted accounting principles in the United States; and
- “PRC GAAP” refers to generally accepted accounting principles in the People’s Republic of China.

This annual report on Form 20-F includes our audited consolidated statements of operation data for the fiscal years ended September 30, 2009, 2010 and 2011 and audited consolidated balance sheet data as of September 30, 2010 and 2011.

Our ADSs, each representing four ordinary shares, are listed on the New York Stock Exchange, Inc., or the NYSE, under the symbol “DL.”

This Annual Report on Form 20-F includes certain registered trademarks, trademarks, and trade names of CDEL, its subsidiaries, its affiliated entities and others. All terms and product names which may be trademarks or registered trademarks of other companies are hereby acknowledged to belong to their respective owners.

## FORWARD-LOOKING STATEMENTS

This annual report on Form 20-F contains forward-looking statements that are based on our current expectations, assumptions, estimates and projections about us and our industry. All statements other than statements of historical fact in this annual report are forward-looking statements. In some cases, these forward-looking statements can be identified by words and phrases such as “may,” “should,” “intend,” “predict,” “potential,” “continue,” “will,” “expect,” “anticipate,” “estimate,” “plan,” “believe,” “is /are likely to” or the negative form of these words and phrases or other comparable expressions. The forward-looking statements included in this annual report relate to, among others:

- our goals and growth strategies;
- our future prospects and market acceptance of our online and offline courses and other products and services;
- our future business development and results of operations;
- projected revenues, profits, earnings and other estimated financial information;
- projected enrollment numbers;
- our plans to expand and enhance our online and offline courses and other products and services;
- competition in the online and offline education and test preparation markets; and
- Chinese laws, regulations and policies, including those applicable to the Internet, Internet content providers, the education and telecommunications industries, mergers and acquisitions, taxation and foreign exchange.

These forward-looking statements involve various risks, assumptions and uncertainties. Although we believe that our expectations expressed in these forward-looking statements are reasonable, our expectations may turn out to be incorrect. Our actual results could be materially different from or worse than our expectations. Important risks and other factors that could cause our actual results to be materially different from our expectations are generally set forth in “Item 3.D. Key Information — Risk Factors,” “Item 5.A. Operating and Financial Review and Prospects – Operating Results – General Factors Affecting Our Results of Operations,” “Item 5.A. Operating and Financial Review and Prospects – Operating Results – Specific Factors Affecting Our Results of Operations,” “Item 11. Quantitative and Qualitative Disclosures About Market Risk,” and elsewhere in this annual report.

The forward-looking statements made in this annual report relate only to events or information as of the date on which the statements are made in this annual report. All forward-looking statements included herein attributable to us or other parties or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We undertake no obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise, after the date of this annual report or to reflect the occurrence of unanticipated events.

## **Market Data and Forecasts**

This annual report also contains data related to China's education, online and offline education, professional education, test preparation and self-education markets that include projections based on a number of assumptions. These markets may not grow at the rates projected by market data, or at all. The failure of these markets to grow at the projected rates may have a material adverse effect on our business prospects, results of operations and the market price of our ADSs. In addition, the relatively new and rapidly changing nature of these markets subjects any projections or estimates relating to the growth prospects or future condition of these markets to significant uncertainties. If any one or more of the assumptions underlying the market data turns out to be incorrect, actual results may differ from the projections based on these assumptions. You should not place undue reliance on these forward-looking statements.

This annual report contains information and statistics relating to China's economy and the industries in which we operate derived from various publications issued by PRC governmental entities which have not been independently verified by us. The information in such official sources may not be consistent with other information compiled in or outside China.

## **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**

#### **A. Selected Consolidated Financial Data**

The following selected consolidated statements of operations data for the fiscal years ended September 30, 2009, 2010 and 2011 (other than ADS data) and the selected consolidated balance sheets data as of September 30, 2010 and 2011 reflect the retrospective adjustment as a result of our decision on September 27, 2011 to discontinue operations of our Gaokao (nationwide college entrance exam) retake preparation and high-school supplementary tutoring business operated by Champion Xinlixiang and the changes to our presentation of statements of operations and balance sheet data starting in fiscal year ended September 30, 2010 following our adoption of Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 810-10-65, *Transition Related to FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51* ("ASC Topic 810-10-65") (collectively, the "Retroactive Adjustments"). They are derived from our audited consolidated financial statements included elsewhere in this annual report and should be read in conjunction with, and are qualified in their entirety by reference to, these consolidated financial statements and related notes. Our selected consolidated statements of operations data for the years ended September 30, 2007 and 2008 and the selected consolidated balance sheets data as of September 30, 2007, 2008 and 2009, except for the impact of the Retroactive Adjustments, are derived from our audited consolidated financial statements. The following information should also be read in conjunction with "Item 5. Operating and Financial Review and Prospects." Our audited consolidated financial statements are prepared in accordance with U.S. GAAP. Our historical results for any prior period are not necessarily indicative of results to be expected for any future period. In addition, due to the Retrospective Adjustments, our results of operations for the years ended September 30, 2007, 2008, 2009, and 2010 and financial positions as of September 30, 2007, 2008, 2009, and 2010 are not directly comparable to the prior reporting periods.

	Years Ended September 30,				
	2007(6)	2008(6)	2009 (adjusted) (6)	2010 (adjusted)(6)	2011(6)
(In thousands of \$, except share, per share and per ADS data)					
<b>Selected Consolidated Statement of Operations Data:</b>					
<b>Net revenues:</b>					
Online education services	10,637	13,900	22,279	23,982	30,788
Books and reference materials	484	1,616	2,709	3,939	4,743
Others	725	2,058	5,133	4,658	6,033
Total net revenues	<u>11,846</u>	<u>17,574</u>	<u>30,121</u>	<u>32,579</u>	<u>41,564</u>
<b>Cost of sales:</b>					
Cost of services <sup>(5)</sup>	(3,553)	(5,981)	(12,834)	(13,283)	(16,840)
Cost of tangible goods sold	(354)	(818)	(1,577)	(2,070)	(2,794)
Total cost of sales	<u>(3,907)</u>	<u>(6,799)</u>	<u>(14,411)</u>	<u>(15,353)</u>	<u>(19,634)</u>
<b>Gross profit</b>	7,939	10,775	15,710	17,226	21,930
<b>Operating expenses:</b>					
Selling expenses <sup>(5)</sup>	(1,285)	(2,448)	(6,722)	(7,176)	(9,771)
General and administrative expenses <sup>(5)</sup>	(1,638)	(3,906)	(7,432)	(10,535)	(12,221)
Impairment of purchased call options	—	—	—	(162)	(1,115)
Total operating expenses	<u>(2,923)</u>	<u>(6,354)</u>	<u>(14,154)</u>	<u>(17,873)</u>	<u>(23,107)</u>
Other operating income	131	209	292	74	603
Other expense	—	(144)	—	—	—
<b>Operating (loss) income</b>	5,147	4,486	1,848	(573)	(574)
Interest income (expense), net	(5)	176	740	458	883
Exchange loss	—	(75)	(6)	(66)	(143)
Equity in loss of an affiliated company	—	(64)	—	—	—
<b>Income (loss) before income taxes</b>	5,142	4,523	2,582	(181)	166
Less: Income tax (expense) benefit	307	(526)	(1,478)	(575)	(971)
Net (loss) income from continuing operations	5,449	3,997	1,104	(756)	(805)
Accretion of Series A convertible contingently redeemable preferred shares to redemption amount and accretion to beneficial conversion feature of Series A convertible contingently redeemable preferred shares	(903)	(9,332)	—	—	—
Net loss of continuing operations attributable to noncontrolling interest	—	—	82	911	303
Net (loss) income from continuing operations attributable to China Distance Education Holdings Limited	4,546	(5,335)	1,186	155	(502)
Net (loss) income from discontinued operations attributable to China Distance Education Holdings Limited, net of tax	—	—	2	(2,053)	(3,300)
<b>Net (loss) income attributable to China Distance Education Holdings Limited</b>	<u>4,546</u>	<u>(5,335)</u>	<u>1,188</u>	<u>(1,898)</u>	<u>(3,802)</u>
<b>Net (loss) income per ordinary share:</b>					
<b>Net(loss) income attributable to China Distance Education Holdings Limited shareholders</b>					
Basic from continuing operations	0.04	(0.05)	0.01	—	—
Basic from discontinued operations	—	—	—	(0.01)	(0.03)
Basic	0.04	(0.05)	0.01	(0.01)	(0.03)
Diluted from continuing operations	0.04	(0.05)	0.01	—	—
Diluted from discontinued operations	—	—	—	(0.01)	(0.03)
Diluted	0.04	(0.05)	0.01	(0.01)	(0.03)
<b>Net (loss) income per ADS:</b>					
<b>Net (loss) income attributable to China Distance Education Holdings Limited shareholders<sup>(1)</sup></b>					
Basic from continuing operations	0.16	(0.20)	0.03	—	(0.01)
Basic from discontinued operations	—	—	—	(0.06)	(0.10)
Basic	0.16	(0.20)	0.03	(0.06)	(0.11)

	Years Ended September 30,				
	2007(6)	2008(6)	2009 (adjusted) (6)	2010 (adjusted)(6)	2011(6)
	(In thousands of \$, except share, per share and per ADS data)				
Diluted from continuing operations	0.16	(0.20)	0.03	—	(0.01)
Diluted from discontinued operations	—	—	—	(0.06)	(0.10)
Diluted	0.16	(0.20)	0.03	(0.06)	(0.11)
<b>Weighted average shares used in calculating net (loss) income per share:</b>					
Basic	95,415,512	100,373,673	140,260,811	138,232,493	133,571,727
Diluted	95,415,512	100,373,673	140,475,941	138,232,493	133,571,727
<b>Other Consolidated Financial Data from Continuing Operations:</b>					
Gross Margin <sup>(2)</sup>	67.0%	61.3%	52.2%	52.9%	52.8%
Operating Margin <sup>(3)</sup>	43.5%	25.5%	6.1%	(1.8)%	(1.4)%
Net Margin <sup>(4)</sup>	46.0%	22.7%	3.9%	0.5%	(1.2)%

- (1) One ADS represents four ordinary shares.
- (2) Gross margin represents gross profit as a percentage of net revenues.
- (3) Operating margin represents operating (loss) income as a percentage of net revenues.
- (4) Net margin represents net (loss) income as a percentage of net revenues.
- (5) Includes the following amounts of share-based compensation expenses for the periods indicated:

	Years Ended September 30,				
	2007	2008	2009	2010	2011
	(in thousands of \$)				
Cost of services	—	689	1,854	1,787	1,999
Selling expenses	—	161	454	567	678
General and administrative expenses	—	629	1,612	2,033	3,347
<b>Total share-based compensation expenses</b>	—	1,479	3,920	4,387	6,024

- (6) The presentation of selected consolidated statements of operations data for the fiscal years ended September 30, 2007, 2008, 2009, 2010 and 2011 reflects the adoption of ASC Topic 810-10-65. In addition, the selected consolidated statements of operations data for the fiscal years ended September 30, 2009 and 2010 have been retrospectively adjusted to reflect the effect of the discontinued operations, where applicable, and are followed by “(adjusted)” where they differ from those reported in our prior year’s annual report on Form 20-F.

	As of September 30,				
	2007(1)	2008(1)	2009(adjusted)(1)	2010(adjusted)(1)	2011(1)
	(in thousands of \$)				
<b>Consolidated Balance Sheet Data:</b>					
Cash and cash equivalents	7,106	66,223	19,091	57,305	49,738
Total assets	19,928	85,326	92,533	95,971	93,878
Deferred revenue	2,524	3,891	6,025	7,545	7,861
Refundable fees	1,907	4,688	1,781	1,564	2,580
Total liabilities	6,241	12,576	15,661	18,948	21,144
Series A convertible contingently redeemable preferred shares	903	—	—	—	—
Total China Distance Education Holdings Limited shareholders’ equity	12,784	72,750	73,909	74,986	72,734
Total liabilities and equity	19,928	85,326	92,533	95,971	93,878

- (1) The presentation of selected consolidated balance sheets data as of September 30, 2007, 2008, 2009, 2010 and 2011 reflects the adoption of ASC Topic 810-10-65. In addition, the selected consolidated balance sheets data as of September 30, 2009 and 2010 have been retrospectively adjusted to reflect the effect of the discontinued operations, where applicable, and are followed by “(adjusted)” where they differ from those reported in our prior year’s annual report on Form 20-F.

## Exchange Rate Information

We use U.S. dollars as our reporting currency in our financial statements and in this annual report. When reporting the operating results and financial position of our PRC subsidiaries and affiliated entities, we use the monthly average exchange rate for the year and the exchange rate at the balance sheet date, respectively, as published by the People's Bank of China. In other parts of this annual report, any Renminbi denominated amounts are accompanied by translations. With respect to amounts not recorded in our consolidated financial statements included elsewhere in this annual report, all translations from Renminbi to U.S. dollars were made at the noon buying rate in the City of New York for cable transfers in Renminbi per U.S. dollar as certified for customs purposes by the Federal Reserve Bank of New York. Unless otherwise noted, all translations from Renminbi to U.S. dollars have been made at RMB6.3780 to \$1.00, the noon buying rate in effect as of September 30, 2011. We make no representation that the Renminbi or U.S. dollar amounts referred to in this annual report could have been or could be converted into U.S. dollars or Renminbi, as the case may be, at any particular rate or at all. The PRC government restricts or prohibits the conversion of Renminbi into foreign currency and foreign currency into Renminbi for certain types of transactions. On February 24, 2012, the noon buying rate was RMB6.2976 to \$1.00.

The following table sets forth information concerning exchange rates between the Renminbi and the U.S. dollar for the periods indicated. These rates are provided solely for your convenience and are not necessarily the exchange rates that we used in this annual report or will use in the preparation of any other information to be provided to you.

	Renminbi per U.S. dollars Noon Buying Rate			
	Average <sup>(1)</sup>	Low	High	Period End
Fiscal year ended September 30, 2007	7.6947	7.9168	7.4928	7.4928
Fiscal year ended September 30, 2008	7.0936	7.5158	6.7800	6.7899
Fiscal year ended September 30, 2009	6.8302	6.8842	6.8171	6.8262
Fiscal year ended September 30, 2010	6.8112	6.8330	6.6869	6.6950
Fiscal year ended September 30, 2011	6.5356	6.6912	6.3778	6.3780
Most recent six months:				
August 2011	6.4036	6.4401	6.3778	6.3778
September 2011	6.3885	6.3975	6.3780	6.3780
October 2011	6.3710	6.3825	6.3534	6.3547
November 2011	6.3564	6.3839	6.3400	6.3765
December 2011	6.3482	6.3733	6.2939	6.2939
January 2012	6.3119	6.3330	6.2940	6.3080
February 2012 (through February 24, 2012)	6.3000	6.3120	6.2938	6.2976

Source: Federal Reserve Bank of New York and U.S. Federal Reserve

- (1) Annual averages are calculated using the exchange rates for the last day of each month during the fiscal year. Monthly averages are calculated using daily exchange rates during the month.

## B. Capitalization and Indebtedness

Not applicable.

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

Not applicable.

## D. Risk Factors

### Risks Relating to Our Business

*If we are unable to continue to attract course participants to enroll in our courses, or to charge our course participants competitive but profitable fees, our revenues may decline and we may not be able to maintain profitability.*



The success of our business depends primarily on the number of enrollments in our courses and the amount of course fees that we can charge. Therefore, our ability to continue to attract course participants to enroll in our courses and charge our course participants competitive but commercially profitable fees is critical to the continued success and growth of our business. This in turn will depend on several factors, including our ability to develop new courses and enhance existing courses to respond to changes in market trends and demands of course participants, to effectively market our courses to a broader base of prospective course participants, to train and retain qualified lecturers and tutors, to develop or acquire additional high-quality educational content and to respond to competitive pressures. In addition, the expansion of our courses, services and products in terms of the types of offerings may not succeed due to competition, our failure to effectively market our new courses, services and products or maintain their quality and consistency, or other factors. For example, with respect to our Gaokao retake preparation and high-school supplementary tutoring business, we have suffered significant operating losses for the fiscal year ended September 30, 2011. As a result, we decided to discontinue such business and put the related assets and business up for sale. Furthermore, we may not be able to develop and offer additional content on commercially reasonable terms and in a timely manner, or at all, to keep pace with changes in market requirements. If we are unable to continue to attract course participants to enroll in our courses, increase enrollments in our relatively new courses, or charge our course participants competitive but profitable fees, our revenues may decline and we may be unable to achieve revenue growth or maintain our profitability.

***If we fail to develop and introduce new courses, services and products that meet our target customers' expectations, or adopt new technologies important to our business, our competitive position and ability to generate revenues may be materially and adversely affected.***

Historically, our core business centered on the provision of online professional education and test preparation courses for accounting professionals. We have since expanded our course offerings to target course participants in the legal, healthcare, construction engineering and other industries, as well as participants of online courses for self-taught learners seeking higher education and other forms of online and offline education. In addition to regular classes, we have also introduced, in the past couple of years, "elite" classes and "premium" classes within some of our most popular course offerings to better serve the needs of high-end customers. The profitability of the elite classes may be subject to risks given that the course participants enjoy refund privileges if certain pre-agreed conditions are met. The profitability of the premium classes may also be subject to risks given that course participants enjoy a 50% discount off the fee of the same courses they may enroll in for the following year if certain pre-agreed conditions are met. The profitability of courses for the examinations of American Institute of CPAs and certain healthcare courses may also be subject to risks given that course participants may retake the same courses free of charge for the following year if certain pre-agreed conditions are met. We also offer business start-up training courses, which are subsidized by governments, to target university students, job seekers and individuals interested in learning to start a business, the profitability of which may be subject to risks given that the subsidy we are entitled to receive from government authorities in certain provinces and cities may be reduced if certain stipulated conditions in the government authorities' subsidy policies are not met. We intend to continue developing new courses, services and products. The timing of the introduction of new courses, services and products is subject to risks and uncertainties.

Unexpected technical, operational, logistical, regulatory or other problems could delay or prevent the introduction of one or more of new courses, services or products. Moreover, we cannot assure you that any of these courses, products and services will match the quality or popularity of those developed by our competitors, achieve widespread market acceptance or generate the desired level of income.

The technology used in Internet and value-added telecommunications services and products in general, and in online education services in particular, and the related technology standards may evolve and change over time. If we fail to anticipate and adapt to such technological changes, our market share and our business development could suffer, which in turn would have a material and adverse effect on our financial condition and results of operations. If we are unsuccessful in addressing any of the risks relating to such new courses, services and products, our business may be materially and adversely affected.

***We may lose market share and our profitability may be materially and adversely affected, if we fail to compete effectively with our present and future competitors or to adjust effectively to changing market conditions and trends.***

We face competition from providers of traditional offline education, training and test preparation services, and expect to face increasing competition from existing competitors and new market entrants in the online professional education and test preparation market. The provision of professional education and test preparation courses over the Internet is a relatively recent concept. Although online education is increasingly perceived as an acceptable means of receiving training and instruction, traditional classroom instruction is still generally viewed as a more accepted method. We therefore compete with traditional in-person educational institutions and training centers in the various subject areas for which we offer courses. As most of our courses are conducted solely online, if the perception that traditional forms of education and training are preferred persists or increases, we may not be able to compete effectively with competitors engaging in traditional forms of education and training. In addition, due to low barriers to entry for Internet-based businesses, we expect to face increasing competition from both existing domestic competitors and new entrants to the online education market. We may face increased competition from international competitors that cooperate with local businesses to provide services based on the foreign partners' technology and experience developed in their home markets. Following our continuous expansion into providing offline courses since 2009, we also face increasing competition from providers of traditional offline education in the various subject areas for which we offer courses.

Our present and future competitors may have longer operating histories, larger student enrollments, larger teams of professional staff and greater financial, technical, marketing and other resources. They may be able to devote more resources to the development and promotion of their courses and services, and may be able to react more quickly to changing customer requirements and demands, deliver competitive services at lower prices or respond to new technologies, trends or user preferences more effectively than we can. They may be able to offer services and products with better performance and prices than ours with the result that their services and products may gain greater market acceptance than ours. They may also offer free promotional services and products in connection with their marketing campaigns or significantly lower the prices for their services and products in order to attract students and capture additional market share. There is no assurance that we will be able to compete effectively with such present and future competitors or to adjust effectively to changing market conditions and trends. Our failure to compete effectively could erode our market share, result in a fall in the number of our course participants, or lead to price reductions or increased spending for marketing and promotion of our courses, any of which may materially and adversely affect our profitability.

***Our business depends on the continued success of our key brand "Chinaacc" and the further enhancement of our newer brands, and if we fail to maintain and enhance recognition of our brands, we may face difficulty in obtaining new business partners and customers, and our business reputation and operating results may be harmed.***

We believe that market awareness of our key brand "Chinaacc" has contributed significantly to the success of our business. Maintaining and enhancing this key brand, further improving our brands in the legal, healthcare and other areas and introducing new brands are critical to our efforts to grow our customer base and obtain additional business partners. However, our main competitors are continuing to take steps to increase their brand recognition. Failure to maintain and enhance our brand recognition could also have a material and adverse effect on our business, operating results and financial condition.

We have initiated brand promotion efforts in recent years, but we cannot assure you that our marketing efforts will be successful in further promoting our brands. If we are unable to further enhance our brand recognition and increase awareness of our courses, services and products, or if we incur excessive marketing and promotion expenses, our business and results of operations may be materially and adversely affected.

***Our business could be adversely affected by changes in the perceived difficulty, requirements or formats of professional examinations and continuing education in China.***

We provide online professional education and test preparation courses relating to the accounting, legal, healthcare, construction engineering and other industries. In addition, we also provide online professional continuing education courses relating to the accounting, healthcare and construction engineering industries. We have obtained approval, and in some cases exclusive rights, to offer self-taught study process monitoring programs in certain provinces and cities, to allow learners to earn up to 30% of the credits they need to obtain post-secondary self-taught education degree. If there is any material change to the perceived difficulty, requirements or formats of examinations and continuing education in these subject areas, and we are unable to modify or supplement our courses or training materials to address these changes in a timely manner, the demand for, and relevance of, our courses and training materials may be adversely affected, which could have an adverse impact on our financial condition and results of operations.

***Our business could be adversely affected by changes in the perceived difficulty, requirements or formats of business start-up training courses, or changes in the government authorities' subsidy policy.***

We provide business start-up training courses, which are sponsored by government authorities, to university students and other job seekers using materials prepared in accordance with requirements of the relevant government authorities in various provinces and cities. We do not charge the course participants fees, instead, we receive payments from the relevant government authorities for courses provided and our net revenue generated from such courses is conditioned on our ability to meet the government stipulated conditions under the subsidy policies. Such policies are established by relevant government authorities in various provinces and cities. When determining our entitlement to the subsidy, the government authorities consider the pass rate of our course participants' business proposals as evaluated by such authorities, as well as the business start-up rate and employment rate of our course participants. If there is any material change to the perceived difficulty, requirements or formats of the courses or the government subsidy policy in relevant provinces and cities, and we are unable to modify or supplement our courses or training materials to address these changes in a timely manner, or to meet the stipulated conditions of the government subsidy policy, the demand for our courses and training materials may decrease and our revenue generated from this course offering may be adversely affected, which could have an adverse impact on our financial condition and results of operations.

***Our business is dependent on our lecturers comprised primarily of academics and experienced practitioners within their respective industries who are typically engaged on a part-time contractual basis, and some of whom are not bound by exclusivity restrictions.***

Most of our courses are conducted by lecturers, comprised primarily of academics from post-secondary educational institutions and experienced practitioners within their respective industries in China. The popularity and effectiveness of our courses depend on the teaching ability of these lecturers and their reputation as skilled lecturers. Our lecturers are typically engaged on a part-time contractual basis for periods ranging from one to three years, except for some more experienced lecturers for whom the contract periods are relatively longer. Most lecturers are not bound by exclusivity restrictions. If our lecturers fail to deliver quality lectures as a result of inadequate devotion of their time and energy to our courses or for other reasons, our business may be adversely affected. In addition, as the online education industry grows and matures, we may face increasing competition from our competitors for lecturers with good reputations and effective teaching skills, and on whom we rely for the delivery of quality services and to maintain and promote our leading market position. Furthermore, some provinces and municipalities where we have business operations including Beijing have promulgated local regulations prohibiting public school teachers from providing paid tutoring services. If our lecturers that are academics from post-secondary educational institutions choose to, or are forced to, discontinue their relationship with us to comply with the relevant local regulations, we will need to seek new lecturers to replace them. We cannot assure you we will be able to find replacements at a reasonable cost on a timely basis, if at all. Any failure to attract qualified lecturers or to maintain or improve the quality of our lectures could adversely affect our reputation and operating results. Additionally, the lecturers may even turn into our competitors after they discontinue their relationship with us, which could further adversely affect our operating results.

***Failure to attract and retain qualified personnel and experienced senior management could disrupt our operations and adversely affect our business and competitiveness.***

Our continuing success is dependent, to a large extent, on our ability to attract and retain qualified personnel and experienced senior management. If one or more of our senior management team members are unable or unwilling to continue to work for us, we may not be able to replace them within a reasonable period of time or at all, and our business may be severely disrupted, our financial condition and results of operations may be materially and adversely affected and we may incur additional expenses in recruiting and training additional personnel. Although our senior management members are subject to certain non-competition restrictions during, and for a period of two years after termination of their employment, we cannot assure you that such non-competition restrictions will be effective or enforceable under PRC law. If any of our senior management joins a competitor or forms a competing business, our business may be severely disrupted. We have no key man insurance with respect to our key personnel that would provide insurance coverage payable to us for loss of their employment due to death or otherwise.

***Zhengdong Zhu, our chairman, chief executive officer and co-founder of our business, has played an important role in the growth and development of our business since its inception, and a loss of his services in the future could severely disrupt our business and negatively affect investor confidence in us, which may also cause the market price of our ADSs to go down.***

Zhengdong Zhu, our chairman, chief executive officer and co-founder of our business, has played an important role in the growth and development of our business since its inception. To date, we have relied heavily on Mr. Zhu's expertise in, and familiarity with, our business operations, his relationships with our employees, and his reputation in the online education industry. In addition, Mr. Zhu continues to be primarily responsible for formulating our overall business strategies and spearheading the growth of our operations. If Mr. Zhu were unable or unwilling to continue in his present positions, we may not be able to easily replace him and may incur additional expenses to identify and train his successor. In addition, if Mr. Zhu were to join a competitor or form a competing business, it could severely disrupt our business and negatively affect our financial condition and results of operations. Although Mr. Zhu is subject to certain non-competition restrictions during, and for a period of two years after termination of, his employment with us, we cannot assure you that such non-competition restrictions will be effective or enforceable under PRC law. Moreover, even if the departure of Mr. Zhu from our company would not have any actual impact on our operations and the growth of our business, it could create the perception among investors or the marketplace that his departure could severely damage our business and operations and could negatively affect investor confidence in us, which may cause the market price of our ADSs to go down. We do not maintain key man insurance on Mr. Zhu.

***Mr. Zhengdong Zhu, our chairman and chief executive officer, beneficially owns a significant percentage of our outstanding ordinary shares and, as a result, he has significantly greater influence over us and our corporate actions relative to our public shareholders and his interests may not be aligned with the interests of other shareholders.***

As of February 24, 2012, our co-founder and chief executive officer, Mr. Zhu, beneficially owned 73,878,493 ordinary shares or approximately 54.43% of our outstanding ordinary shares. Mr. Zhu is an affiliate as defined in Rule 144 under the Securities Act of 1933, as amended, or the Securities Act, due to the large size of his shareholding in us and his positions with us as our chairman and chief executive officer. Rule 144 defines an affiliate of a company as a person that, directly or indirectly, through one or more intermediaries, controls or is controlled by, or is under common control with, our company. Mr. Zhu has, and may continue to have, significant influence in determining the outcome of any corporate transactions or other matters submitted to our shareholders for approval, including mergers, consolidations and the sale of all or substantially all of our assets, election of directors and other significant corporate actions. He may not act in the best interests of our minority shareholders. In addition, without the consent of Mr. Zhu, we could be prevented from entering into transactions that could be beneficial to us. This concentration of ownership may also discourage, delay or prevent a change in control of our company, which could deprive our shareholders of an opportunity to receive a premium for their shares as part of a sale of our company and might reduce the price of our ADSs. These actions may be taken even if they are opposed by our other shareholders. Furthermore, we engaged in related party transactions with Mr. Zhu and entities controlled by Mr. Zhu in the past. For example, we rented our office premises located at Xueyuan International Tower in Beijing from Mr. Zhu from 2004 to 2007, and purchased such office premises from Mr. Zhu in 2007 at mutually agreed prices. However, we cannot assure you that such transactions have always been conducted on an arms' length basis or on terms that are most favorable to us and our shareholders.

***Our business is subject to seasonal fluctuations, which may cause our operating results to fluctuate from quarter to quarter. This may result in volatility in and adversely affect the price of our ADSs.***

We have experienced seasonality and expect in the future to continue to experience seasonality in revenues related to the provision of our education courses primarily due to seasonal changes in course enrollments and the timing of various exams. We typically open new online courses to enrollment approximately six months before the relevant exam date. As the majority of our course participants take non-refundable courses relating to the main professional accounting exams, which are typically held in May and September, we historically have experienced higher revenues during the quarters ending June 30 and September 30 of each fiscal year. With respect to our refundable courses, which is also primarily related to the main professional accounting exams, we typically recognize revenues 15 days after the release of the relevant exam results when the participants' applicable refund privileges expire, resulting in higher revenues in the quarter ended March 31 and September 30. With respect to our professional continuing education courses, we typically recognize revenues when course participants complete the stipulated study hours and take the examinations, or on a straight line basis over the subscription period, starting from a course participant's enrollment date, ranging from three months to one year. As the majority of our course participants take accounting professional continuing education courses in the second half of the calendar year, we historically have experienced higher revenues during the quarters ending September 30 and December 31 of each fiscal year. As a result, we historically have generated higher revenue in the second half of each fiscal year. These fluctuations could result in volatility and adversely affect the price of our ADSs. As our revenues grow, these seasonal fluctuations may become more pronounced.

***Our failure to protect our intellectual property rights may undermine our competitive position, and litigation to protect our intellectual property rights or defend against third party allegations of infringement may be costly and ineffective.***

We believe that our copyrights, trademarks and other intellectual property are instrumental to our success. We depend to a large extent on our ability to develop and maintain the proprietary aspects of our technology and products. We have devoted considerable time and energy to the development and improvement of our websites, our online training platform and our training courses and materials.

We rely primarily on copyrights, trademarks, trade secrets, unpatented proprietary technologies, processes and know-how and other contractual restrictions to protect our intellectual property. Nevertheless, these provide only limited protection and the actions we take to protect our intellectual property rights may not be adequate. Our trade secrets may become known or be independently discovered by our competitors. Third parties may infringe upon or misappropriate our proprietary technologies or other intellectual property rights, which could have a material adverse effect on our business, financial condition or operating results. Policing the unauthorized use of proprietary technology can be difficult and expensive. Also, litigation may be necessary to enforce our intellectual property rights, protect our trade secrets or determine the validity and scope of the proprietary rights of others. The outcome of such potential litigation may not be in our favor and any success in litigation may not be able to adequately protect our rights. Such litigation may be costly and divert management's attention away from our business. An adverse determination in any such litigation would impair our intellectual property rights and may harm our business, prospects and reputation. Enforcement of judgments in China is uncertain, and even if we are successful in litigation, it may not provide us with an effective remedy. In addition, we have no insurance coverage against litigation costs and would have to bear all costs arising from such litigation to the extent we are unable to recover them from other parties. The occurrence of any of the foregoing could have a material adverse effect on our business, financial condition and results of operations.

***We may be exposed to infringement claims by third parties or held liable for defamation or negligence to third parties for information displayed on, retrieved from or linked to our websites, based on the content of the books and reference materials or marketing materials that we or our lecturers author or distribute or for information delivered or shared through our services, which could disrupt our business and cause us to incur substantial legal costs, or damage our reputation.***

We cannot assure you that our services and products do not or will not infringe any intellectual property rights held by third parties. We have in the past, in the ordinary course of business, experienced claims for intellectual property infringement, none of which has had a material effect on our business. We cannot assure you that in the future we would not receive claims of infringement of third parties' proprietary rights or claims for indemnification resulting from infringement arising from our services or products. We may also become subject to claims that content on our websites or in the books and reference materials or marketing materials that we or our lecturers author or distribute is in fact protected by third parties' copyright ownership rights or trademark.

In addition, as a provider of Internet content and other value-added telecommunications services, we may face liability for defamation, negligence and other claims based on the nature and contents of the materials that are displayed on our websites or delivered or shared through our services. We could also be subject to claims based upon content that is accessible on our websites or through our networks, such as content and materials posted by visitors on message boards, online communities, email or chat rooms offered on our websites. By providing hypertext links to third-party websites, we may be held liable for copyright or trademark violations by those third-party websites. Third parties could assert claims against us for losses incurred in reliance on any erroneous information distributed by us.

Royalty or licensing agreements, if required, may not be available on acceptable terms, if at all. A successful claim of infringement against us and our failure or inability to obtain a license to use the infringed or similar technology or content on commercially acceptable terms, or at all, could prevent us from producing and offering our services or products or cause us to incur great expense and delay in developing non-infringing services or products. Any of the above events could in turn have a material and adverse impact on our financial condition and results of operations. Any defamation or negligence claims against us, even if they do not result in liability to us, could cause us to incur significant costs in investigating and defending against these claims. We do not have general liability insurance to cover all potential claims to which we are exposed, and our insurance coverage may not be adequate to indemnify us from all liability that may be imposed.

***Concerns about the security of our transaction systems and confidentiality of information on the Internet may reduce use of our services and impede our growth.***

Public concerns over the security and privacy of electronic settlement, online transmittal and communications have significantly constrained the rapid development and expansion of online transactions. If these concerns are not adequately addressed, they will restrict the growth of value-added telecommunications services generally, and in particular the use of the Internet as a means of conducting commercial transactions. If a well-publicized breach of security were to occur, general usage of telecommunications value-added services could decline, which could reduce our visitor traffic and the number of course participants, and impede our growth. We have not experienced any material cyber attacks on our information technology systems and are continuously vigilant about protecting and improving our cyber security. We cannot assure you, however, that our current security measures will be adequate or sufficient to prevent any theft or misuse of personal data of our course participants. Further, security breaches could expose us to litigation and possible liability for failing to secure confidential customer information, and could harm our reputation and ability to attract or retain course participants. In addition, we do not have any cyber security insurance coverage for our operations, and any material cyber attack on our information technology systems and our online education websites could expose us to substantial costs and losses.

***The successful operation of our business depends upon the performance and reliability of the Internet infrastructure and telecommunications networks in China.***

Our business depends on the performance and reliability of the Internet infrastructure in China. Almost all access to the Internet is maintained through state-controlled telecommunications operators. In addition, the national networks in China are connected to the Internet through international gateways controlled by the PRC government. These international gateways are generally the only channels through which a domestic user can connect to the Internet. We cannot assure you that a more sophisticated Internet infrastructure will be developed in China. We may not have access to alternative networks in the event of disruptions, failures or other problems with China's Internet infrastructure. In addition, the Internet infrastructure in China may not support the demands associated with continued growth in Internet usage.

We also rely on China Telecommunications Corporation, or China Telecom, China United Network Communications Group Co., Ltd., or China Unicom, and China Tie Tong Telecommunications Corporation, or China Tie Tong, to provide us with data communications capacity primarily through local telecommunications lines and Internet data centers to host our servers. We do not have access to alternative services in the event of disruptions, failures or other problems with the telecommunications networks of China Telecom, China Unicom and China Tie Tong or if they otherwise fail to provide such services. Any unscheduled service interruption could disrupt our operations, damage our reputation and result in a decrease in our revenues.

Furthermore, we have no control over the costs of services provided by China Telecom, China Unicom and China Tie Tong. If the prices that we pay for telecommunications and Internet services rise significantly, our gross profit and net income could be adversely affected. In addition, if Internet access fees or other charges to Internet users increase, our visitor traffic may decrease, which in turn may harm our revenues.

***Unexpected network interruptions, security breaches or computer virus attacks and system failures could have a material adverse effect on our business, financial condition and results of operations.***

Any failure to maintain satisfactory performance, reliability, security or availability of our network infrastructure may cause significant damage to our reputation and our ability to attract and maintain course participants. Major risks involving our network infrastructure include:

- breakdowns or system failures resulting in a prolonged shutdown of our servers, including failures attributable to power shutdowns, or attempts to gain unauthorized access to our systems, which may cause loss or corruption of data or malfunctions of software or hardware;
- disruption or failure in the national backbone network, which would make it impossible for visitors and course participants to log on to our websites;
- damage from fire, flood, power loss and telecommunications failures; and
- any infection by or spread of computer virus.

Any network interruption or inadequacy that causes interruptions in the availability of our websites or deterioration in the quality of access to our websites could reduce customer satisfaction and result in a reduction in the number of course participants using our services. If sustained or repeated, these performance issues could reduce the attractiveness of our websites and course offerings. In addition, any security breach caused by hackings, which involve attempts to gain unauthorized access to information or systems, or to cause intentional malfunctions or loss or corruption of data, software, hardware or other computer equipment, could cause a disruption in our services. Inadvertent transmission of computer viruses could expose us to a material risk of loss of our course files or litigation and possible liability, as well as damage to our reputation.

Furthermore, increases in the volume of traffic on our websites could also strain the capacity of our existing computer systems, which could lead to slower response times or system failures. This would cause a disruption or suspension in our course offerings, which would hurt our brand and reputation, and thus negatively affect our revenue growth. We may need to incur additional costs to upgrade our computer systems in order to accommodate increased demand if we anticipate that our systems cannot handle higher volumes of traffic in the future.

All of our servers and routers, including backup servers, are currently hosted by third-party service providers in multiple cities in China. We do not maintain any backup servers outside of these cities. To improve the performance and to prevent disruption of our services, we may have to make substantial investments to deploy additional servers or one or more copies of our websites to mirror our online resources.

***We may continue to grant share options and/or restricted shares under our current or future share incentive plans, or modify the terms of existing share options, which may continue to materially impact our future results of operations or result in dilution to our shareholders.***

We adopted our Share Incentive Plan in April 2008, the Prior Plan, under which we have to date granted options for the purchase of a total of 11,045,500 ordinary shares to selected officers, employees, and lecturers. We adopted in July 2008, and amended and restated in February 2009, our 2008 Performance Incentive Plan, or the New Plan, under which we reserved a maximum number of 11,267,992 ordinary shares as of September 30, 2011, plus an automatic annual adjustment. Pursuant to the New Plan, we have to date granted options for the purchase of a total of 3,162,500 ordinary shares, and issued 157,143 restricted shares, to selected directors, and employees. In addition, on September 27, 2011, we revised the exercise price of 8,066,700 and 1,398,300 options under the Prior Plan from \$0.82 to \$0.615, which equaled the per share value of our ADS on the NYSE at the close of trading on September 27, 2011, and zero per share, respectively. Furthermore, the re-priced options had been accelerated to be fully vested on the same day. See “Item 6.B. Directors, Senior Management and Employees — Compensation — Share Options, Restricted Shares and Share Incentive Plan.” In connection with the share options we granted and restricted shares we issued, we incurred \$3.9 million, \$4.4 million and \$6.0 million of share-based compensation expenses in the fiscal years ended September 30, 2009, 2010 and 2011, respectively, see “Item 5.A. Operating and Financial Review and Prospects — Operating Results — Share-based Compensation Expenses.” The expenses associated with options granted and restricted shares issued under the share incentive plans may continue to materially impact our future results of operations. In addition, if we grant additional options, restricted shares and other equity incentives in the future under our current or future share incentive plans, or modify the terms of existing share options, we could further incur significant share-based compensation expenses, or experience a reduction in our net income. Such actions could also result in dilution to our shareholders.

***We may need additional capital but may not be able to obtain it on acceptable terms or at all.***

We believe that our current cash and cash equivalents and anticipated cash flows from operations will be sufficient to meet our anticipated working capital requirements and capital expenditures for at least the next 12 months. We do not anticipate that our current expansion plans will require significant capital commitments due to the scalability of our business model. We do, however, expect to spend money on the further development of our “Chinaacc” brand and other brands in the disciplines for which we offer courses. We do not expect our short-term and long-term cash requirements to be materially different.

Nevertheless, we may require additional sources of liquidity in the event of changes in business conditions or other future developments. Factors affecting our sources of liquidity include, for example, mergers and acquisitions, our sales performance, ability to control costs and expenses, and choice of financing arrangements. Any changes in the significant factors affecting our revenues from education services may cause material fluctuations in our cash generated from operations. See “Item 5.A. Operating and Financial Review and Prospects — Operating Results — Overview — Specific Factors Affecting Our Results of Operations” for a description of these significant factors. Changes in working capital, including any significant shortening or lengthening of our accounts receivable cycle or client prepayment cycles, may also cause fluctuations in our cash generated from operations. If our sources of liquidity are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities to meet our cash needs. The sale of convertible debt securities or additional equity securities could result in dilution to our shareholders. The incurrence of indebtedness would result in debt service obligations and could result in operating and financial covenants that restrict our operations. Our ability to obtain additional capital on acceptable terms is subject to a variety of uncertainties, including:

- investors’ perception of, and demand for, securities of companies mainly providing online professional education and test preparation courses;
- conditions of the U.S. and other capital markets in which we may seek to raise funds;
- our future results of operations, financial condition and cash flows;
- PRC governmental regulation of foreign investment in Internet, educational services and professional training services companies;
- economic, political and other conditions in China; and
- PRC governmental policies relating to foreign currency borrowings.

We cannot assure you that financing will be available in amounts or on terms acceptable to us, if at all. Any failure by us to raise additional funds on terms favorable to us, or at all, could have a material adverse effect on our business, financial condition and results of operations.

***We may not be able to effectively manage the expansion of our operations through new acquisitions or joint ventures or to successfully realize the anticipated benefits of any such acquisition or joint venture.***

We have historically complemented our organic growth through the selective acquisition of complementary businesses, assets, products or technology, or the formation of joint ventures, and we may continue to do so in the future. The identification of suitable acquisition targets or joint venture candidates can be difficult, time consuming and costly, and we may not be able to successfully capitalize on identified opportunities. Consummation of acquisitions and the subsequent integration of new assets and businesses into our own could also be costly and require significant attention from our management and could result in a diversion of resources from our existing business, which in turn could have an adverse effect on our business operations. Acquired assets or businesses may not generate the financial results we expect and may even result in our suffering losses. For example, with respect to our acquisition of business start-up training business in March 2009, we sought through arbitration to require the vendors, among other things, to compensate us for the loss incurred as a result of their failure to perform the related agreement. For more information regarding the arbitration, please see “Item 8. Financial Information—Legal Proceedings.” With respect to our acquisition of Gaokao retake preparation and high-school supplementary tutoring business in September 2009, we have suffered significant operating losses for the fiscal year ended September 30, 2011 and decided to discontinue such business and put the related assets and business up for sale. Moreover, completions of acquisitions are typically subject to various approval processes. In addition to possible shareholders’ approval, we may also have to obtain approvals and licenses from the relevant government authorities in the PRC for the acquisitions and to comply with any applicable PRC laws and regulations, which could result in increased costs and delay. Furthermore, acquisitions or joint ventures could result in the use of substantial amounts of cash, potentially dilutive issuances of equity or equity-linked securities or the incurrence of debt, the incurrence of significant goodwill, intangible assets and other long-term assets impairment charges, amortization expenses for other intangible assets and exposure to potential unknown liabilities of the acquired business, or other charges, any of which could have a material adverse effect on our business, financial condition and results of operations.

***Our operations could be disrupted by an outbreak of fire or other calamities and we have limited insurance coverage.***

We store books and audio and visual products at our premises to support our courses. As such, there is a risk that these products and our premises may be damaged or destroyed by fire and other natural calamities. Any disruption of electricity supply or any outbreak of fire or similar calamities at our premises may result in the breakdown of our facilities and disruption to our business. In addition, any fire or other calamity at the facilities of our third-party service providers that host our servers could severely disrupt our ability to deliver our courses and other services over our websites.

At present, insurance companies in the PRC offer limited coverage for business related risks. As such, we only have a very limited form of insurance for our property covering loss of property arising from theft, fire, lightning, explosives and damage caused by aerial objects. We do not have any business liability or disruption insurance coverage for our operations, and our coverage may not be adequate to compensate for all losses that may occur, particularly with respect to loss of business and reputation. Any business disruption, litigation or natural disaster could expose us to substantial costs and losses.

***Our financial performance and prospects could be affected by natural calamities or health epidemics.***

Our business could be materially and adversely affected by natural calamities or health epidemics such as influenza, severe acute respiratory syndrome or other epidemics. On May 12, 2008, a major earthquake struck China's populous Sichuan province and was felt across much of the country, causing great loss of life, numerous injuries, property loss and disruption to the local economy. The earthquake had an immediate impact on our business as a result of an announcement by the Ministry of Finance to postpone the administration of the Elementary Level and Intermediate Level Accounting Professional Qualification Exams across China as a direct result of the earthquake, which exams were originally scheduled to be held on the third weekend of May 2008. On July 2, 2008, the Ministry of Finance announced that these exams will be held on September 6 and 7, 2008. As a result of the exam dates being rescheduled from May 2008 to September 2008, deferred revenue generated from our test preparation courses relating to the two major accounting exams was not fully recognized as revenue by May 2008, but were recognized over a longer period of time through September 2008. In addition, refundable fees relating to these two exams were not recognized as revenue in the fiscal fourth quarter ended September 30, 2008 and were instead recognized in the fiscal first quarter ended December 31, 2008 when the exam results were released. For a more detailed discussion of how we recognize revenues, see "Item 5.A. Operating and Financial Review and Prospects — Operating Results — Critical Accounting Policies — Revenue Recognition." In addition, in recent years, there were reports regarding the occurrences of various forms of influenza in different parts of China, including cases resulting in deaths. Any occurrences of natural calamities or epidemics may result in the postponement or rescheduling of examinations for which we provide courses, which may in turn have an adverse impact on our revenues and performance. In addition, if our employees are affected by natural calamities or contagious or virulent diseases, we may fail to provide our courses, materials and services in a timely manner, which will have an adverse impact on our financial performance. We have not adopted any written preventive measures or contingency plans to combat any future natural calamities or outbreak of epidemics. Any natural calamities or prolonged recurrence of adverse public health developments in China may have a material and adverse effect on our business operations, financial performance and prospects.

***We may be exposed to liability for our course content, information or advice we provide to our course participants or customers of our other services.***

We may be subject to legal claims from our course participants or customers of our other services for losses they suffer if such losses arise from their reliance on content, information or advice that we provide to them. Such claims, with or without merit, may be expensive to defend and may have an adverse impact on our reputation. Further, if such claims are successful, we may be held liable to pay compensation which may in turn adversely affect our financial condition and results of operations.

***Failure to maintain effective internal control over financial reporting could have a material and adverse effect on the trading price of our ADSs.***

We are subject to the reporting obligations under the U.S. securities laws. The Securities and Exchange Commission, or the SEC, as required under Section 404 of the Sarbanes-Oxley Act, has adopted rules requiring every public company to include a report of management on the effectiveness of such companies' internal control over financial reporting in its annual report, which contains management's assessment of the effectiveness of the company's internal control over financial reporting. In addition, an independent registered public accounting firm must issue an attestation report on the effectiveness of the company's internal control over financial reporting. These requirements apply to our annual report on Form 20-F for the fiscal year ended September 30, 2011.



Our management has concluded that our internal control over financial reporting was effective as of September 30, 2011. Our independent registered public accounting firm has issued an attestation report, which has concluded that we maintained, in all material aspects, effective internal control over financial reporting as of September 30, 2011. See “Item 15. Controls and Procedures.” However, if we fail to maintain effective internal control over financial reporting in the future, our management and our independent registered public accounting firm may not be able to conclude that we have effective internal control over financial reporting at a reasonable assurance level. This could negatively affect the reliability of our financial information and result in the loss of investors’ confidence in our reported financial information, which in turn could negatively impact the trading price of our ADSs. Furthermore, we have incurred and anticipate that we will continue to incur considerable costs, management time and other resources in an effort to comply with Section 404 and other requirements of the Sarbanes-Oxley Act.

## **Risks Relating to Our Corporate Structure and Restrictions on Our Industry**

***Substantial uncertainties and restrictions exist with respect to the interpretation and application of PRC laws and regulations relating to the distribution of Internet content in China. If the PRC government finds that the structure we have adopted for our business operations does not comply with PRC laws and regulations, we could be subject to severe penalties, including the shutting down of our websites.***

Foreign ownership of Internet-based businesses is subject to significant restrictions under current PRC laws and regulations. The PRC government regulates Internet access, the distribution of online information and the conduct of online commerce through strict business licensing requirements and other government regulations. These laws and regulations also include limitations on foreign ownership in PRC companies that provide Internet content distribution services. Specifically, foreign investors are not allowed to own more than 50% equity interests in any entity conducting Internet content distribution business.

Because we are a Cayman Islands company and we hold the equity interests of our PRC subsidiaries indirectly through China Distance Education Limited, a Hong Kong company, or CDEL Hong Kong, our PRC subsidiaries are treated as foreign invested enterprises under PRC laws and regulations. To comply with PRC laws and regulations, we conduct our operations in China through a series of contractual arrangements entered into among CDEL Hong Kong, our two PRC subsidiaries, Beijing Champion Distance Education Technology Co., Ltd., or Champion Technology and Beijing Champion Education Technology Co., Ltd. or Champion Education Technology, our affiliated PRC entity, Beijing Champion and its shareholders. Beijing Champion is a PRC limited liability company 79% owned by Zhengdong Zhu, our chairman and chief executive officer and a major shareholder, and 21% owned by Baohong Yin, our co-founder and deputy chairman, both of whom are PRC citizens. Beijing Champion holds a Telecommunications and Information Services Operating License, or ICP license, issued by the Beijing Telecommunications Administration Bureau, a local branch of China’s Ministry of Industry and Information, or MII, which allows Beijing Champion to provide Internet content distribution services. Each of Beijing Caikaowang Company Limited, or Caikaowang, Beijing Champion Wange Education Technology Co., Ltd., or Champion Wange, and Beijing Zhengbao Yucai Education Technology Co., Ltd., or Zhengbao Yucai, is a subsidiary of Beijing Champion, and holds an ICP license issued by the Beijing Telecommunications Administration Bureau. Beijing Champion and its subsidiaries have also received approvals issued by the Beijing Telecommunications Administration Bureau to provide online bulletin board services on 13 of our 17 websites where we currently provide such services. In addition, Beijing Champion holds a Permit of Internet Cultural Activities issued by the Ministry of Culture, which permits Beijing Champion to engage in production and dissemination of cultural products through the Internet. The ICP licenses and other approvals held by Beijing Champion and its subsidiaries are essential to the operation of our business.

As a result of these contractual arrangements, we control Beijing Champion and its subsidiaries and, accordingly, under U.S. GAAP, we consolidate its operating results in our financial statements. For a description of these contractual arrangements, see “Item 4.C. Information on the Company — Organizational Structure.”

The relevant PRC regulatory authorities have broad discretion in determining whether a particular contractual structure is in violation of law. For example, on July 26, 2006, MII issued the Notice on Intensifying the Administration of Foreign Investment in Value-added Telecommunications Services, or the MII Notice. The MII Notice prohibits a domestic telecommunications service provider from leasing, transferring or selling telecommunications business operating licenses to any foreign investor in any form, or providing any resources, sites or facilities to any foreign investor for its illegal operation of a telecommunications business in China. According to the MII Notice, either the holder of a value-added telecommunications service license or its shareholders must directly own the domain names and trademarks used by such license holder in its provision of value-added telecommunications services. The MII Notice also requires each license holder to have the necessary facilities, including servers, for its approved business operations and to maintain such facilities in the regions covered by its license. In order to comply with the MII Notice, we have transferred all domain names and trademarks that are primarily used in connection with our online business activities from Champion Technology to Beijing Champion.

Furthermore, if our ownership structure, contractual arrangements and businesses of our company, our PRC subsidiaries and Beijing Champion or its subsidiaries are found to be in violation of any existing or future PRC laws or regulations, the relevant regulatory authorities would have broad discretion in dealing with such violations, including:

- revoking the business and operating licenses of our PRC subsidiaries or Beijing Champion or its subsidiaries, which business and operating licenses are essential to the operation of our business;
- levying fines;
- confiscating our income or the income of our PRC subsidiaries or Beijing Champion or its subsidiaries;
- shutting down our servers or blocking our websites;
- discontinuing or restricting our operations or the operations of our PRC subsidiaries or Beijing Champion or its subsidiaries;
- imposing conditions or requirements with which we, our PRC subsidiaries or Beijing Champion or its subsidiaries may not be able to comply;
- requiring us, our PRC subsidiaries or Beijing Champion or its subsidiaries to restructure our relevant ownership structure, operations or contractual arrangements; and
- taking other regulatory or enforcement actions that could be harmful to our business.

If the regulatory authorities take any of the above-mentioned measures against us, we may have to cease our business operations and our reputation will be severely damaged, which in turn will materially and negatively affect our financial condition and results of operations.

***Our contractual arrangements may be subjected to severe censorship under PRC laws and regulations and, thus, be challenged by relevant regulatory authorities.***

On February 3, 2011, the General Office of the State Council issued the Circular of the General Office of the State Council on the Establishment of Security Review System for Foreign Investors' Merger and Acquisition of Domestic Enterprises (the "Circular on the Establishment of Security Review"), which became effective on March 4, 2011. Among other things, the Circular on the Establishment of Security Review stipulates that the scope of the security review lies in foreign investors' acquisition of domestic military enterprises, military-related enterprises, enterprises involving sensitive military facilities and other enterprises that impact national defense security; foreign investors' acquisition of domestic enterprises which may provide foreign investors with de facto control over industries relating to national security, such as important agricultural products, energy and natural resources, infrastructures, transportation services, technologies and major equipment manufacturing. On August 25, 2011, the Ministry of Commerce issued the Circular of the Ministry of Commerce on the Implementation of Security Review System for Foreign Investors' Merger and Acquisition of Domestic Enterprises (the "Circular on the Implementation of Security Review"), which became effective on September 1, 2011. Among other things, the Circular on the Implementation of Security Review further specifies that whether a foreign investors' acquisition of domestic enterprises falls within the scope of the security review depends on the said transaction's substantive content and practical influence. Foreign investors shall not circumvent the security review through any arrangements or schemes, including but not limited to trust, lease and/or contractual arrangements.

According to our PRC counsel, as our contractual arrangements were established in 2003, the new security review system shall not apply to our contractual arrangements. We cannot guarantee, however, that the Ministry of Commerce will not promulgate additional implementing rules or new rules that will bring our contractual arrangements under the scope of the security review system. Moreover, according to a press conference held by the Ministry of Commerce on September 20, 2011, there are no specific laws or regulations governing contractual arrangements like the ones that we employ, but the Ministry of Commerce together with other authorities would study how to regulate them in the future. Hence, we cannot assure you that our contractual arrangements will not be subject to new regulations that will be issued by relevant regulatory authorities and that such new regulations will not cause any material adverse effect on our existing structure.

***We rely on contractual arrangements with our affiliated PRC entity and its shareholders for our China operations, which may not be as effective in providing operating control as direct ownership. If any of Beijing Champion or its shareholders fails to perform its or their obligations under these contractual arrangements, we may have to legally enforce such arrangements and our business, financial condition and results of operations may be materially and adversely affected if these arrangements cannot be enforced.***

PRC laws and regulations restrict foreign ownership in Internet-related content distribution businesses. Because of these restrictions, we conduct our business and derive related revenues through contractual arrangements among CDEL Hong Kong, our PRC subsidiaries, Beijing Champion, and its shareholders, Zhengdong Zhu and Baohong Yin. We have no direct ownership interest in Beijing Champion. These contractual arrangements may not be as effective in providing us with control over Beijing Champion as direct ownership. If we were the controlling shareholder of Beijing Champion with direct ownership, we would be able to exercise our rights as shareholders to effect changes in the board of directors, which in turn could implement changes, subject to any applicable fiduciary obligations, at the management level. However, under the current contractual arrangements, as a legal matter, if Beijing Champion fails to perform its obligations under these contractual arrangements, we may have to (i) incur substantial costs and resources to enforce such arrangements, and (ii) rely on legal remedies under PRC law, including contract remedies, which we cannot be sure would be effective. In the event that we are unable to enforce these contractual arrangements, or if we suffer significant time delays or other obstacles in the process of enforcing these contractual arrangements, our business, financial condition and results of operations could be materially and adversely affected.

***Due to the lack of relevant interpretation and implementation of law, we may not be able to register changes to our pledge rights over the equity interests of Beijing Champion held by its shareholders, which may result in inadequate protection of our rights and adverse impact on our contractual arrangements with Beijing Champion.***

Our contractual arrangements with Beijing Champion include equity pledge agreements pursuant to which each of the shareholders of Beijing Champion has pledged all of his or her equity interests in Beijing Champion to Champion Technology as security for the performance of Beijing Champion's obligations under the technical support and consultancy services agreement. According to the PRC Property Rights Law, which became effective on October 1, 2007, pledge rights for a pledge of equity are created at the time of registration of the pledge with the State Administration for Industry and Commerce, or SAIC, or its local office. According to the Measures Regarding Equity Pledge Registration issued by SAIC on September 1, 2008, which became effective on October 1, 2008, any change to the number of shares pledged, the name of the pledgor or pledgee and the name of the enterprise whose equity is pledged shall be registered with SAIC or its local office. We successfully registered the pledges created under the equity pledge agreements with the Beijing office of SAIC on January 12, 2009 and have not experienced any changes to the pledged equity interests since that would require us to update the registration. However, if any change occurs to the pledges created under the equity pledge agreements in the future, including without limitation any change to the number of shares pledged thereunder due to any increase or transfer of the registered capital of Beijing Champion or otherwise, we need to update our equity pledge registration with SAIC or its local office. However, due to the lack of relevant interpretation and implementation of laws, we cannot assure you that we will be able to successfully update our equity pledge registration with SAIC or its local office in connection with any change to the pledges created under our equity pledge agreements. If we fail to update our equity pledge registration in respect of any change to the pledges created under the equity pledge agreements, the protection of our rights under such agreements may become inadequate and our contractual arrangements with Beijing Champion may be adversely impacted.

***The shareholders of Beijing Champion may have potential conflicts of interest with us, which may materially and adversely affect our business and financial condition.***

Zhengdong Zhu and Baohong Yin are husband and wife, and shareholders of Beijing Champion, holding equity interests of 79% and 21%, respectively. The interest of Zhengdong Zhu and Baohong Yin as shareholders of Beijing Champion may differ from our interests. Although both of Zhengdong Zhu and Baohong Yin have given undertakings to act in the best interests of Champion Technology, we cannot assure you that when conflicts arise, these individuals will act in our best interests or that conflicts will be resolved in our favor.

***We may lose the ability to use and enjoy assets held by Beijing Champion and its subsidiaries that are important to the operation of our business if any of such entities goes bankrupt or becomes subject to a dissolution or liquidation proceeding.***

As part of our contractual arrangements with Beijing Champion, Beijing Champion and its subsidiaries hold certain assets that are important to the operation of our business. If Beijing Champion or any of its subsidiaries goes bankrupt and all or part of their assets become subject to liens or rights of third-party creditors, we may be unable to continue some or all of our business activities, which could materially and adversely affect our business, financial condition and results of operations. If Beijing Champion or any of its subsidiaries undergoes a voluntary or involuntary liquidation proceeding, the unrelated third-party creditors may claim rights to some or all of these assets, thereby hindering our ability to operate our business, which could materially and adversely affect our business, financial condition and results of operations.

***Contractual arrangements we have entered into among our subsidiaries and Beijing Champion may be subject to scrutiny by the PRC tax authorities and a finding that we or Beijing Champion owe additional taxes could substantially reduce our consolidated net income.***

Under PRC laws and regulations, arrangements and transactions among related parties may be subject to audit or challenge by the PRC tax authorities. We could face material and adverse tax consequences if the PRC tax authorities determine that the contractual arrangements and transactions among our subsidiaries and Beijing Champion do not represent an arm's length price and adjust the income of our subsidiaries or that of Beijing Champion in the form of a transfer pricing adjustment. A transfer pricing adjustment could, among other things, result in a reduction, for PRC tax purposes, of expense deductions recorded by Beijing Champion, which could in turn increase its respective tax liabilities. In addition, the PRC tax authorities may impose late payment fees and other penalties on our affiliated entities for underpayment of taxes. Our consolidated net income may be materially and adversely affected if our affiliated entities' tax liabilities increase or if it is found to be subject to late payment fees or other penalties.

***We may rely principally on dividends and other distributions on equity paid by our PRC subsidiaries for our cash requirements, but such dividends and other distributions are subject to restrictions under PRC law. Limitations on the ability of our PRC subsidiaries to transfer funds to us could materially and adversely affect our ability to grow, make investments or acquisitions, pay dividends, and otherwise fund and conduct our businesses.***

Current PRC regulations permit our PRC subsidiaries to pay dividends to us only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. However, our PRC subsidiaries are required under PRC laws and regulations to allocate a portion of their annual after-tax profits, if any, to certain statutory reserves and funds prior to declaring and remitting dividends. For example, our PRC subsidiaries are required to allocate at least 10% of their after-tax profits to statutory reserves until such reserves reach 50% of their respective registered capital. Allocations to these statutory reserves and funds can be used only for specific purposes and are not transferable to us in the form of loans, advances or cash dividends. As a result, our PRC subsidiaries are restricted in their ability to transfer a portion of their net assets to us.

***If any of our affiliated entities fails to obtain and maintain the requisite licenses and approvals held by it under the complex regulatory environment for Internet-based businesses in China, our business, financial condition and results of operations may be materially and adversely affected.***

The Internet industry in China is highly regulated by the PRC government. Various regulatory authorities of the central PRC government, such as the State Council, MII, the State Administration of Industry and Commerce, the State Press and Publication Administration, the State Administration of Radio, Film and Television, or SARFT, and the Ministry of Public Security, are empowered to issue and implement regulations governing various aspects of the Internet industry.

Each of our affiliated entities including Beijing Champion, Caikaowang, Zhengbao Yucai and Champion Wangge is required to obtain and maintain applicable licenses or approvals from different regulatory authorities in order to provide its current services. Our affiliated entities have obtained primary approvals including an ICP license for our 17 websites and an approval for operating electronic bulletin board services on 13 websites where we currently provide such services. These licenses are essential to the operation of our business and are generally subject to annual review by the relevant governmental authorities. Our affiliated entities, however, may be required to obtain additional licenses, such as an Internet Publishing License for engaging in Internet publishing and an Internet News Information Services Provision Approval for engaging in distribution of news through the Internet. If any of our affiliated entities fails to obtain or maintain any of the required licenses or approvals, its continued business operations in the Internet industry may subject it to various penalties, such as confiscation of illegal revenues, fines and the discontinuation or restriction of its operations. Any such disruption in the business operations of our affiliated entities will materially and adversely affect our business, financial condition and results of operations.

***If we are unable to re-register or obtain the necessary license as required by the Administrative Measures Regarding Internet Audio-Video Program Services, or the Internet Audio-Video Program Measures, promulgated in 2007 in a timely manner or at all, our equity ownership structure may require significant restructuring, or we may become subject to significant penalties, fines, legal sanctions or an order to suspend our use of audio-video content, in which case our business, financial condition and results of operations may be materially and adversely affected.***

On December 20, 2007, SARFT and MII issued the Internet Audio-Video Program Measures, which became effective on January 31, 2008. Among other things, the Internet Audio-Video Program Measures stipulate that no entities or individuals may provide Internet audio-video program services without a License for Disseminating Audio-Video Programs through Information Network issued by SARFT or its local counterparts or completing the relevant registration with SARFT or its local counterparts and only entities wholly owned or controlled by the PRC government may engage in the production, editing, integration or consolidation, and transfer to the public through the Internet, of audio-video programs, and the provision of audio-video program uploading and transmission services. On February 3, 2008, SARFT and MII jointly held a press conference in response to inquiries related to the Internet Audio-Video Program Measures, during which SARFT and MII officials indicated that providers of audio-video program services established prior to the promulgation date of the Internet Audio-Video Program Measures that do not have any regulatory non-compliance records can re-register with the relevant government authorities to continue their current business operations. After the conference, the two authorities published a press release that confirms the above guidelines. On September 15, 2009, SARFT promulgated a notice regarding the issues of management of Internet Audio-Video Program Services License, which provide that the application for re-registration of the Internet Audio-Video Program Services License shall be closed on December 20, 2009.

Due to uncertainties with respect to the interpretation and application of the Internet Audio-Video Program Measures, each year, we and our PRC counsel consult the Beijing Branch of SARFT, or Beijing SARFT, which is the competent authority in Beijing to grant the License for Disseminating Audio-Video Programs through Information Network, by way of face-to-face interview or telephone consultation regarding whether online education services providers like us that provide audio-video educational courses and programs through the Internet only to enrolled course participants should apply for said license. The officials in Beijing SARFT replied verbally in 2008, 2009 and early 2010 that we were not required to apply for said license as we are an education service provider that only transmits audio-video educational courses and programs through the Internet to enrolled course participants instead of the general public. However, when we consulted Beijing SARFT again in January 2011, Beijing SARFT indicated that the scope of application of the Internet Audio-Video Program Measures was expanded by SARFT to cover educational course providers like us and thus we are required to apply for the License for Disseminating Audio-Video Programs through Information Network. Further to the application scope expansion, in January 2011, a joint administrative enforcement commission of the Beijing government (including Beijing SARFT) issued a warning to us and fined us RMB6,000 (\$897) for providing audio-video educational courses without obtaining the License for Disseminating Audio-Video Programs through Information Network. After the consultation, we began to apply to Beijing SARFT for said license. After accepting our application in February 2011, Beijing SARFT sent us a written reply on March 8, 2011. According to the reply, due to the special circumstance that we have been involved in the distance education industry for many years and our websites www.chinaacc.com, www.chinalawedu.com, and www.ck100.com had been approved by the Ministry of Education and the related telecommunication authority before the promulgation of Internet Audio-Video Program Measures, Beijing SARFT would further deliberate our application and officially respond to us thereafter. On August 1, 2011, Beijing SARFT sent us another written reply which states that Beijing SARFT had consulted with SARFT and determined that the License for Disseminating Audio-Video Programs through Information Network is not applicable to us as basic education, higher education, teacher education, vocational education, adult education, and distance education activities do not fall under the “Internet audio-visual services program.” Therefore, we are not required to obtain the License for Disseminating Audio-Video Programs. We cannot guarantee that Beijing SARFT will not change its position or that the reply will not be challenged by higher authorities in China, or that we will not be asked to obtain the said license again. If the regulatory authorities take any such actions against us, it may materially and adversely affect our business. Moreover, if we are asked to re-register with relevant authorities or obtain the required license, we cannot assure you that our future application(s) will be approved by relevant authorities in a timely manner or at all. If we are subsequently required to and are unable to re-register or obtain the necessary license timely, or at all, due to reasons beyond our control, our equity ownership structure may require significant restructuring, or we may become subject to significant penalties, fines, legal sanctions or an order to suspend our use of audio-video content, any of which could have a material adverse effect on our business, financial condition, results of operations, and prospects, as well as the trading price of our ADSs.

***Regulation and censorship of information distribution 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.***

China has enacted laws and regulations governing Internet access and the distribution of news, information, audio-video programs or other contents, as well as products and services, through the Internet. In the past, the PRC government has prohibited the distribution of information through the Internet that it deems in violation of PRC laws and regulations. Under regulations promulgated by the State Council, MII, the State Press and Publication Administration and the Ministry of Culture, Internet content providers and Internet publishers are prohibited from posting or displaying over the Internet content that, among other things:

- opposes the fundamental principles of the PRC constitution;
- compromises state security, divulges state secrets, subverts state power or damages national unity;
- harms the dignity or interests of the state;
- incites ethnic hatred or racial discrimination or damages inter-ethnic unity;
- sabotages China’s religious policy or propagates heretical teachings or feudal superstition;
- disseminates rumors, disturbs social order or disrupts social stability;
- propagates obscenity, pornography, gambling, violence, murder, fear or abets the commission of crimes;
- insults or slanders a third party or infringes upon the lawful rights of a third party; and
- includes other content prohibited by laws or regulations.

If any of our Internet content were deemed by the PRC government to violate any of the above content restrictions, we would not be able to continue to display such content and could become subject to penalties, including confiscation of income, fines, suspension of business and revocation of required licenses, which could materially and adversely affect our business, financial condition and results of operations. We may also be subject to potential liability for any unlawful actions of our clients or affiliates or for content we distribute that is deemed inappropriate. It may be difficult to determine the type of content that may result in liability to us, and if we are found to be liable, we may be prevented from operating our websites in China.

## **General Risks Relating to Conducting Business in China**

***PRC economic, political and social conditions, as well as changes in any government policies, laws and regulations, could adversely affect the overall economy in China or the prospects of the education market, which in turn could adversely affect our business.***

Substantially all of our operations are conducted in China, and substantially all of our revenues are derived from China. Accordingly, our business, financial condition, results of operations, prospects and certain transactions we may undertake are subject, to a significant extent, to economic, political and legal developments in China.

The PRC economy differs from the economies of most developed countries in many respects, including the amount of government involvement, level of development, growth rate, control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth in the past two to three decades, growth has been uneven, both geographically and among various sectors of the economy. Demand for our products and services depends, in large part, on economic conditions in China. Any slowdown in China's economic growth may cause our potential customers to delay or cancel their plans to participate in our education courses, which in turn could reduce our net revenues.

Although the PRC economy has been transitioning from a planned economy to a more market-oriented economy since the late 1970s, the PRC government continues to play a significant role in regulating industry development by imposing industrial policies. The PRC government also exercises significant control over China's economic growth through the allocation of resources, controlling the incurrence and payment of foreign currency-denominated obligations, setting monetary policy and providing preferential treatment to particular industries or companies. Changes in any of these policies, laws and regulations could adversely affect the overall economy in China or the prospects of the education market, which could harm our business.

The PRC government has implemented various measures to encourage foreign investment and sustainable economic growth and to guide the allocation of financial and other resources. While some of these measures benefit the overall PRC economy, they may also have a negative effect on us. For example, our financial condition and results of operations may be adversely affected by government control over capital investments or changes in tax regulations that are applicable to us. As the PRC economy is increasingly intricately linked to the global economy, it is affected in various respects by downturns and recessions of major economies around the world, such as the recent financial services and economic crises of these economies. The various economic and policy measures the PRC government adopts to forestall economic downturns or shore up the PRC economy may adversely affect our business. We cannot assure you that the PRC government will not repeal or alter these measures or introduce new measures that will have a negative effect on us.

China's social and political conditions are also not as stable as those of the United States and other developed countries. Any sudden changes to China's political system or the occurrence of widespread social unrest could have negative effects on our business and results of operations. In addition, China has tumultuous relations with some of its neighbors and a significant further deterioration in such relations could have negative effects on the PRC economy and lead to changes in governmental policies that would be adverse to our business interests.

***The PRC legal system embodies uncertainties that could limit the legal protections available to you and us.***

Unlike common law systems, the PRC legal system is based on written statutes and decided legal cases have little precedential value. In 1979, the PRC government began to promulgate a comprehensive system of laws and regulations governing economic matters in general. The overall effect of legislation since then has been to significantly enhance the protections afforded to various forms of foreign investment in China. Our PRC operating subsidiaries, Champion Technology and Champion Education Technology, are wholly foreign-owned enterprises, and both are subject to laws and regulations applicable to foreign investment in China in general and laws and regulations applicable to wholly foreign-owned enterprises in particular. Our PRC affiliated entities, Beijing Champion, Caikaowang, Champion Wangge, Beijing Haidian District Champion Training School, or Champion Training School, Zhengbao Yucai, and Champion Xinlixiang, are subject to laws and regulations governing the formation and conduct of domestic PRC companies. Relevant PRC laws, regulations and legal requirements may change frequently, and their interpretation and enforcement involve uncertainties. For example, we may have to resort to administrative and court proceedings to enforce the legal protection that we enjoy either by law or contract. However, since PRC administrative and court authorities have significant discretion in interpreting and implementing statutory and contractual terms, it may be more difficult to evaluate the outcome of administrative and court proceedings and the level of legal protection we enjoy than under more developed legal systems. Such uncertainties, including the inability to enforce our contracts and intellectual property rights, could materially and adversely affect our business and operations. Accordingly, we cannot predict the effect of future developments in the PRC legal system, particularly with respect to the education sector, including the promulgation of new laws, changes to existing laws or the interpretation or enforcement thereof, or the preemption of local regulations by national laws. These uncertainties could limit the legal protections available to us and other foreign investors.

***Fluctuations in exchange rates could result in foreign currency exchange losses.***

We report our financial results in U.S. dollars, and appreciation or depreciation in the value of the Renminbi (which is the currency in which substantially all of our revenues and expenditures are denominated) relative to the U.S. dollar would affect our financial results reported in U.S. dollars terms without giving effect to any underlying change in our business or results of operations. Fluctuations in the exchange rate will also affect the relative value of any dividend we issue that will be exchanged into U.S. dollars and earnings from and the value of any U.S. dollar-denominated investments we make in the future.

The Renminbi's exchange rate with the U.S. dollar and other currencies is affected by, among other things, changes in China's political and economic conditions and China's foreign exchange policies. The People's Bank of China regularly intervenes in the foreign exchange market to limit fluctuations in Renminbi exchange rate and achieve certain exchange rate targets, and through such intervention kept the U.S. dollar-Renminbi exchange rate relatively stable between 6.8 and 6.9 Renminbi per U.S. dollar for almost two years from July 2008. On June 20, 2010, the People's Bank of China announced that the PRC government would further reform the Renminbi exchange rate regime and increase the flexibility of the exchange rate. Under China's current exchange rate regime, the Renminbi may appreciate or depreciate significantly in value against the U.S. dollar in the medium to long term. There remains significant international pressure on the PRC government to adopt a substantial liberalization of its currency policy, which could result in a further and more significant appreciation in the value of the Renminbi against the U.S. dollar.

Very limited hedging transactions are available in China to reduce our exposure to exchange rate fluctuations. 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 availability and effectiveness of these hedging transactions may be limited and we may not be able to successfully hedge our exposure at all. In addition, our currency exchange losses may be magnified by PRC exchange control regulations that restrict our ability to convert Renminbi into foreign currency.

***The discontinuation of any of the preferential tax treatments currently available to our PRC subsidiary, Champion Technology, and affiliated entity, Beijing Champion, could materially increase our tax liabilities.***

Prior to January 1, 2008, under applicable PRC tax laws, companies established in China were generally subject to an enterprise income tax, or EIT, at the statutory rate of 33%. However, certain types of foreign-invested enterprises and high and new technology enterprises located in certain specified high-tech zones were entitled to preferential tax treatments. Under the then applicable PRC tax laws, each of our two PRC subsidiaries, Champion Technology and Champion Education Technology, had been granted preferential EIT treatment based on their status as foreign-invested enterprises and their status as high and new technology enterprises operating in Beijing Zhongguancun Science Park. Our PRC affiliated entity, Beijing Champion had been granted preferential EIT treatment based on its status as a high and new technology enterprise operating in the Zhongguancun Science Park.

In March 2007, the National People's Congress enacted the Enterprise Income Tax Law, or the New EIT Law, and in December 2007, the State Council promulgated the implementing rules of the New EIT Law, both of which became effective on January 1, 2008. The New EIT Law significantly curtails tax incentives granted to foreign-invested enterprises under the previous tax law. The New EIT Law, however, (i) reduces the statutory rate of enterprise income tax from 33% to 25%, (ii) permits companies to continue to enjoy their existing tax incentives, subject to certain transitional phase-out rules, and (iii) introduces new tax incentives, subject to various qualification criteria. Under the phase-out rules, enterprises established before the promulgation date of the New EIT Law and which were granted preferential EIT treatment under the then effective tax laws or regulations may continue to enjoy their preferential tax treatments until their expiration. Accordingly, Champion Technology, an enterprise established before the promulgation date of the New EIT Law, continued to enjoy its preferential treatment under the phase-out rules, whereas Champion Education Technology, established after the promulgation date, was no longer entitled to its preferential treatment as of January 1, 2008. The New EIT Law and its implementing rules permit qualified "high and new technology enterprises" to enjoy a reduced 15% EIT rate. The qualification criteria are significantly higher than those prescribed by the old tax rules under which we had been granted preferential treatment. Champion Education Technology is no longer entitled to the 15% reduced tax rate and became subject to the statutory 25% EIT rate as of January 1, 2008 because it does not qualify under the new criteria. Beijing Champion and Champion Technology obtained the qualification certificates of high and new technology enterprises under the New EIT Law on December 24, 2008 with a valid period of three years starting from January 1, 2008. As a result, Beijing Champion is subject to the tax rate of 15% from 2008 through 2010. Champion Technology is subject to the tax rate of 7.5% for 2008 through 2009 and 15% for 2010. However, the continued qualification of a high and new technology enterprise will be subject to annual evaluation and a three-year review by the relevant government authority in China. Beijing Champion and Champion Technology obtained the qualification certificates of high and new technology enterprises under the New EIT Law on October 11, 2011 again. As a result, Beijing Champion and Champion Technology are subject to the tax rate of 15% from 2011 to 2013. The PRC tax policies, interpretations, and practices regarding the overlap, phase-out, and transition of preferential treatments is subject to continuous change and uncertainty and we cannot assure you that Beijing Champion and Champion Technology will continue to qualify as high and new technology enterprises under the New EIT Law, enjoy the preferential treatments under the phase-out rules, not encounter any challenges regarding past application of such treatments, or that the local tax authorities will not, in the future, change their position and revoke any of our past preferential tax treatments. The discontinuation of any of our preferential tax treatments could materially increase our tax obligations.

Any increase in the enterprise income tax rate applicable to us or discontinuation or reduction of any of the preferential tax treatments currently enjoyed by our PRC subsidiary, Champion Technology, and affiliated entity, Beijing Champion, could adversely affect our business, operating results and financial condition.

***Under China's New EIT Law, we may be classified as a "resident enterprise" of China. Such classification could result in unfavorable tax consequences to us and our non-PRC shareholders.***

Under the New EIT Law, an enterprise established outside of China with "de facto management bodies" within China is considered a "resident enterprise," and will generally be subject to the uniform 25% PRC enterprise income tax rate on its global income. The implementing rules of the New EIT Law define de facto management as "substantial and overall management and control over the production and operations, personnel, accounting, and properties" of the enterprise. A circular issued by the State Administration of Taxation (the "SAT") on April 22, 2009 provides that a foreign enterprise controlled by a PRC company or a PRC company group will be classified as a "resident enterprise" with its "de facto management bodies" located within China if the following requirements are satisfied: (i) the senior management and core management departments in charge of its daily operations function are mainly in the PRC; (ii) its financial and human resources decisions are subject to determination or approval by persons or bodies in the PRC; (iii) its major assets, accounting books, company seals, and minutes and files of its board and shareholders' meetings are located or kept in the PRC; and (iv) at least half of the enterprise's directors with voting right or senior management reside in the PRC.

Our management is currently based in China and expected to remain in China. Although CDEL Cayman as our holding company is not controlled by a PRC company or company group, we cannot assure you that CDEL Cayman will not be deemed to a "resident enterprise" under the New EIT Law and its implementation rules. The "resident enterprise" rule could be applied to CDEL Hong Kong as our intermediate holding company and Practice Enterprises Network China International Links Limited, or PENCIL with similar consequences. If the PRC tax authorities determine that CDEL Cayman, CDEL Hong Kong and PENCIL are "resident enterprises" for PRC enterprise income tax purposes, a number of unfavorable PRC tax consequences could follow. First, we may be subject to enterprise income tax at a rate of 25% on our worldwide taxable income, as well as PRC enterprise income tax reporting obligations. Second, although under the New EIT Law and its implementing rules, a dividend income between qualified resident enterprises is a "tax-exempt income," we cannot guarantee that dividends paid to CDEL Cayman from our PRC subsidiaries through CDEL Hong Kong would qualify as "tax-exempt income" and will not be subject to withholding tax, as the PRC foreign exchange control authorities, which enforce the withholding tax, have not yet issued guidance with respect to the processing of outbound remittances to entities that are treated as "resident enterprises" for PRC enterprise income tax purposes. Finally, the new "resident enterprise" classification could result in a situation in which a 10% withholding tax is imposed on dividends we pay to our non-PRC enterprise shareholders and with respect to gains derived by our non-PRC enterprise shareholders from transferring our shares or ADSs, if such income is considered PRC-sourced income by the relevant PRC authorities. This could have the effect of increasing our and our shareholders' effective income tax rates and could also have an adverse effect on our net income and results of operations, and may require us to deduct withholding tax amounts from any dividends we pay to our non-PRC shareholders.

In addition to the uncertainty in how the new "resident enterprise" classification could apply, it is also possible that the rules may change in the future, possibly with retroactive effect. We are actively monitoring the possibility of "resident enterprise" treatment for the 2012 tax year and are evaluating appropriate organizational changes to avoid this treatment, to the extent possible.

***If the China Securities Regulatory Commission, or CSRC, or another PRC regulatory agency determines that its approval was required in connection with our initial public offering, we may become subject to penalties.***

On August 8, 2006, six PRC regulatory agencies, including the CSRC, promulgated the Regulation on Mergers and Acquisitions of Domestic Companies by Foreign Investors, or the M&A Rule, which became effective on September 8, 2006, and was amended on June 22, 2009. The M&A Rule, among other things, has certain provisions that require offshore special purpose vehicles, or SPVs, formed for the purpose of acquiring PRC domestic companies and controlled by PRC individuals, to obtain the approval of the CSRC prior to listing their securities on an overseas stock exchange. We believe, based on the opinion of our PRC legal counsel, Jingtian & Gongcheng, that while the CSRC generally has jurisdiction over overseas listings of SPVs like us, CSRC's approval was not required for our initial public offering given the fact that our current corporate structure was established before the new regulation became effective. However, there remains some uncertainty as to how this regulation will be interpreted or implemented in the context of an overseas offering. If the CSRC or another PRC regulatory agency subsequently determines that its approval was required for our initial public offering, we may face sanctions by the CSRC or another PRC regulatory agency. If this happens, these regulatory agencies may impose fines and penalties on our operations in the PRC, limit our operating privileges in the PRC, delay or restrict the injection of the proceeds from our initial public offering into our PRC subsidiaries, restrict or prohibit payment or remittance of dividends by our PRC subsidiaries to us or take other actions that could have a material adverse effect on our business, financial condition, results of operations, reputation and prospects, as well as the trading price of our ordinary shares.



***The M&A Rule establishes more complex procedures for some acquisitions of PRC companies by foreign entities, which could make it more difficult for us to pursue growth through acquisitions in China.***

The M&A Rule establishes additional procedures and requirements that could make some acquisitions of PRC companies by foreign entities, such as ours, more time-consuming and complex, including requirements in some instances that the Ministry of Commerce be notified in advance of any change-of-control transaction in which a foreign entity takes control of a PRC domestic enterprise. In the future, we may grow our business in part by acquiring complementary businesses. Complying with the requirements of the M&A Rule to complete such transactions could be time-consuming, and any required approval processes, including obtaining approval from the Ministry of Commerce, may delay or inhibit our ability to complete such transactions, which could affect our ability to expand our business or maintain our market share.

***PRC regulation of loans and direct investment by offshore holding companies to PRC entities may restrict our ability to make loans to our PRC subsidiaries and PRC affiliated entities or to make additional capital contributions to our PRC subsidiaries, which could materially and adversely affect our liquidity and our ability to fund and expand our business.***

We are an offshore holding company conducting our operations in China through our PRC subsidiaries and our PRC affiliated entities, Beijing Champion, Caikaowang, Champion Wangge, Champion Training School, Zhengbao Yucai and Champion Xinlixiang. From time to time, we plan to make loans to our PRC subsidiaries, whether currently in existence or to be formed in the future, and to our PRC affiliated entities, whether currently in existence or to be formed in the future, or make additional capital contributions to our PRC subsidiaries.

Any loans we make to our PRC subsidiaries cannot exceed statutory limits and must be registered with the State Administration of Foreign Exchange, or SAFE, or its local counterparts. Under applicable PRC law, the government authorities must approve a foreign-invested enterprise's registered capital amount, which represents the total amount of capital contributions made by the shareholders that have been registered with the registration authorities. In addition, the authorities must also approve the foreign-invested enterprise's total investment, which represents the total statutory capitalization of the company, equal to the company's registered capital plus the amount of loans it is permitted to borrow under the law. The ratio of registered capital to total investment cannot be lower than the minimum statutory requirement and the excess of the total investment over the registered capital represents the maximum amount of borrowings that a foreign invested enterprise is permitted to have under PRC law. If we were to make loans to our PRC subsidiaries, we would have to apply to the relevant government authorities for an increase in their permitted total investment amounts. The various applications could be time-consuming and their outcomes may be uncertain. Furthermore, even if we make loans to our PRC subsidiaries that do not exceed their current maximum amount of borrowings, we will have to register each loan with SAFE or its local counterpart for the issuance of a registration certificate of foreign debts. In practice, it could be time-consuming to complete such SAFE registration process. Concurrently with the loans, we might have to make capital contributions to these subsidiaries to maintain the statutory minimum registered capital and total investment ratio, and such capital contributions involve uncertainties of their own. Further, SAFE promulgated another circular (known as Circular 142) in August 2008 with respect to the administration of conversion of foreign exchange capital contributions of a foreign invested enterprise. The circular clarifies that Renminbi converted from foreign exchange capital contributions can only be used for the activities within the approved business scope of such foreign invested enterprise and cannot be used for domestic equity investments unless otherwise permitted.

Because our PRC affiliated entities are domestic PRC entities, we are not likely to finance their activities by means of direct capital contributions due to regulatory issues relating to foreign investment in the online education industry, as well as the licensing and other regulatory issues discussed in "Item 4.B. Information on the Company — Business Overview — Regulations." Any loans we make to any of our PRC affiliated entities, which is treated as a PRC domestic company rather than a foreign-invested enterprise under PRC law, are also subject to various PRC regulations and approvals. Under applicable PRC regulations, international commercial loans to PRC domestic companies are subject to various government approvals.

We cannot assure you that we will be able to complete the necessary government registrations or obtain the necessary government approvals on a timely basis, if at all, with respect to future loans by us to our PRC subsidiaries or PRC affiliated entities or with respect to future capital contributions by us to our PRC subsidiaries. If we fail to complete such registrations or obtain such approvals, our ability to capitalize or otherwise fund our PRC operations may be negatively affected, which could adversely and materially affect our liquidity and our ability to fund and expand our business.

***A failure by our shareholders or beneficial owners who are PRC citizens or residents to comply with certain PRC foreign exchange regulations could restrict our ability to distribute profits, restrict our overseas and cross-border investment activities or subject us to liability under PRC laws, which could adversely affect our business and financial condition.***

In October 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-Raising and Return Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies, or SAFE Circular 75. According to SAFE Circular 75, prior to establishing or assuming control of an offshore enterprise for the purpose of financing that offshore enterprise with assets or equity interests in an onshore enterprise in the PRC, each PRC resident, whether a natural or legal person, must complete certain overseas investment foreign exchange registration procedures with the relevant local SAFE branch. An amendment to the registration with the local SAFE branch is required to be filed by any PRC resident that directly or indirectly holds interests in that offshore enterprise upon either (i) the injection of equity interests or assets of an onshore enterprise to the offshore enterprise or (ii) any overseas fund-raising by such offshore enterprise after such injection. An amendment to the registration with the local SAFE branch is also required to be filed by such PRC resident when there is any material change involving a change in the capital of the offshore enterprise, such as (i) an increase or decrease in its capital, (ii) a transfer or swap of shares, (iii) a merger or division, (iv) a long-term equity or debt investment or (v) the creation of any security interests. Under subsequent SAFE rules, PRC subsidiaries of an offshore enterprise governed by SAFE Circular 75 are required to coordinate and supervise the filing of SAFE registrations in a timely manner by the offshore holding company's shareholders who are PRC residents. If these shareholders fail to comply, the PRC subsidiaries are required to report to the local SAFE authorities. If our shareholders who are PRC citizens or residents do not complete their registration with the local SAFE authorities, our PRC subsidiaries will be prohibited from distributing their profits and proceeds from any reduction in capital, share transfer or liquidation to us, and we may be restricted in our ability to contribute additional capital to our PRC subsidiaries. Mr. Zhengdong Zhu is in the process of completing the requisite SAFE Circular 75 registration in connection with the transaction that occurred in October 2011 among Bertelsmann Asia Investment AG, Champion Shine Trading Limited ("CST") and Champion Education Holdings Limited ("CEH"). See "Item 6. E. Share Ownership — Historical Changes in Shareholdings of our Major Shareholders" for more details.

We are committed to complying, and to ensuring that our shareholders, who are PRC citizens or residents, comply with the SAFE Circular 75 requirements. However, we may not at all times be fully aware or informed of the identities of all our beneficial owners who are PRC citizens or residents, and we may not always be able to compel our beneficial owners to comply with the SAFE Circular 75 requirements. As a result, we cannot assure you that all of our shareholders or beneficial owners who are PRC citizens or residents will at all times comply with, or in the future make or obtain any applicable registrations or approvals required by, SAFE Circular 75 or other related regulations. Failure by any such shareholders or beneficial owners to comply with SAFE Circular 75 could subject us to fines or legal sanctions, restrict our overseas or cross-border investment activities, limit our subsidiaries' ability to make distributions or pay dividends or affect our ownership structure, which could adversely affect our business and prospects.

***We may be subject to fines and legal sanctions imposed by SAFE or other Chinese government authorities if we or our Chinese employees fail to comply with Chinese regulations relating to employee share options granted by offshore listed companies to Chinese citizens.***

In March 2007, SAFE issued the Application Procedure of Foreign Exchange Administration for Domestic Individuals Participating in Employee Share Holding Plan or Share Option Plan of Overseas Listed Company, or the Share Option Rule. Under the Share Option Rule, Chinese citizens who are granted share options by an offshore listed company are required, through a Chinese agent or Chinese subsidiary of the offshore listed company, to register with the SAFE and complete certain other procedures, including applications for foreign exchange purchase quotas and opening special bank accounts. We and our Chinese employees who have been granted share options are subject to the Share Option Rule. If we or our Chinese employees fail to comply with these regulations, we or our Chinese employees may be subject to fines and legal sanctions imposed by the SAFE or other Chinese government authorities, which may prevent us from further granting options under our share incentive plans to our employees. Such events could adversely affect our business operations. See "Item 4.B. Information on the Company — Business overview — Regulations — SAFE Regulations on Employee Share Options."

***Restrictions on currency exchange may limit our ability to utilize our revenues effectively and the ability of our PRC subsidiaries to obtain financing.***

Substantially all of our revenues and operating expenses are denominated in Renminbi. Restrictions on currency exchange imposed by the PRC government may limit our ability to utilize revenues generated in Renminbi to fund our business activities outside China, if any, or expenditures denominated in foreign currencies. Under current PRC regulations, Renminbi may be freely converted into foreign currency for payments relating to “current account transactions,” which include among other things dividend payments and payments for the import of goods and services, by complying with certain procedural requirements. Our PRC subsidiaries may also retain foreign exchange in their respective current account bank accounts, subject to a cap set by SAFE or its local counterpart, for use in payment of international current account transactions.

However, conversion of Renminbi into foreign currencies, and of foreign currencies into Renminbi, for payments relating to “capital account transactions,” which principally includes investments and loans, generally requires the approval of SAFE and other relevant PRC governmental authorities. Restrictions on the convertibility of the Renminbi for capital account transactions could affect the ability of our PRC subsidiaries to make investments overseas or to obtain foreign exchange through debt or equity financing, including by means of loans or capital contributions from us.

Any existing and future restrictions on currency exchange may affect the ability of our PRC subsidiaries or affiliated entities to obtain foreign currencies, limit our ability to utilize revenues generated in Renminbi to fund our business activities outside China that are denominated in foreign currencies, or otherwise materially and adversely affect our business.

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

We conduct substantially all of our operations in China and substantially all of our assets other than a majority of cash and cash equivalents are located in China. In addition, most of our directors and executive officers reside outside the United States. As a result, it may be difficult to effect service of process upon us or our directors or executive officers. In addition, you may find it difficult or impossible to bring an action against us or our directors or executive officers in a PRC court if you believe your rights have been infringed under the U.S. federal securities law or otherwise. Moreover, our PRC counsel has advised us that China does not have treaties with the United States or many other countries providing for the reciprocal recognition and enforcement of court orders.

**Risks Relating to Our ADSs**

***Stock prices of companies with business operations primarily in China have fluctuated widely in recent years, and the trading prices of our ADSs are likely to be volatile, which could result in substantial losses to investors.***

The trading prices of our ADSs are likely to be volatile and could fluctuate widely in response to factors beyond our control. For example, if one or more of the industry analysts or ratings agencies who cover us downgrades us or our ADSs, the price of our ADSs may decline. If one or more of these analysts or agencies cease to cover our company or fail to regularly publish reports on us, we could lose visibility in the financial markets, which could cause the price of our ADSs or trading volume to decline. In addition, the performance and fluctuation of the market prices of other technology companies with business operations mainly in China that have listed their securities in the United States may affect the volatility in the price of and trading volumes for our ADSs. In recent years, a number of PRC companies have listed their securities, or are in the process of preparing for listing their securities, on U.S. stock markets. Some of these companies have experienced significant volatility, including significant price declines following their initial public offerings. The trading performances of these PRC companies’ securities at the time of or after their offerings may affect the overall investor sentiment towards PRC companies listed in the United States and consequently may impact the trading performance of our ADSs. These broad market and industry factors may significantly affect the market price and volatility of our ADSs, regardless of our actual operating performance.

In addition to market and industry factors, the price and trading volume for our ADSs may be highly volatile for specific business reasons. Factors such as variations in our revenues, earnings and cash flow, announcements of new investments, cooperation arrangements, acquisitions, cessation of business lines or legal disputes including arbitration, and fluctuations in market prices for our services could cause the market price for our ADSs to change substantially. Any of these factors may result in large and sudden changes in the volume and price at which our ADSs will trade. We cannot give any assurance that these factors will not occur in the future again. In the past, following periods of volatility in the market price of a company’s securities, shareholders have often instituted securities class action litigation against that company. If we were involved in a class action lawsuit, it could divert the attention of senior management, and, if adversely determined, could have a material adverse effect on our business, financial condition and results of operations.

***The sale or availability for sale of substantial amounts of our ADSs could adversely affect their market price.***

Sales of substantial amounts of our ADSs in the public market, or the perception that these sales could occur, could adversely affect the market price of our ADSs and could materially impair our future ability to raise capital through offerings of our ADSs. As of September 30, 2011, there were 127,800,673 ordinary shares outstanding. All of our ADSs are freely tradable without restriction or further registration under the Securities Act unless held by our “affiliates” as that term is defined in Rule 144 under the Securities Act. Subject to the applicable restrictions and limitations under Rule 144 of the Securities Act, all of our shares outstanding are eligible for sale in the public market. In addition, as of September 30, 2011, there were 12,488,012 outstanding options to purchase ordinary shares out of which 10,851,056 outstanding options have vested under their current terms. If these additional shares are sold, or if it is perceived that they will be sold in the public market, the trading price of our ordinary shares could decline.

***Anti-takeover provisions in our organizational documents may discourage our acquisition by a third party, which could limit your opportunity to sell your shares at a premium.***

Our second amended and restated memorandum of association and articles of association include provisions that could limit the ability of others to acquire control of us, modify our structure or cause us to engage in change of control transactions, including, among other things, the following:

- provisions that restrict the ability of our shareholders to call meetings and to propose special matters for consideration at shareholder meetings;
- provisions that authorize our board of directors, without action by our shareholders, to issue preferred shares and to issue additional ordinary shares, including ordinary shares represented by ADSs; and
- provisions that provide for a staggered board, whereby our board will be divided into three classes of directors, with directors in each class serving staggered three-year terms. With a staggered board, at least two annual shareholders’ meetings, instead of one, would generally be required to effect a change in a majority of the board. A staggered board tends to discourage proxy contests for the election of directors and purchases of a substantial block of shares because a staggered board operates to prevent a third party from obtaining control of our board in a relatively short period of time. See “Item 6.C. Directors, Senior Management and Employees — Board Practices.”

These provisions could have the effect of depriving you of an opportunity to sell your ADSs at a premium over prevailing market prices by discouraging third parties from seeking to acquire control of us in a tender offer or similar transactions.

***The voting rights of holders of ADSs must be exercised in accordance with the terms of the deposit agreement, and the procedures established by the depositary. The process of voting through the depositary may involve delays that limit the time available to you to consider proposed shareholders’ actions and also may restrict your ability to subsequently revise your voting instructions.***

A holder of ADSs may exercise its voting rights with respect to the underlying ordinary shares only in accordance with the provisions of the deposit agreement. When the depositary receives from us notice of any shareholders meeting, it will distribute the information in the meeting notice and any proxy solicitation materials to you. The depositary will determine the record date for distributing these materials, and only ADS holders registered with the depositary on that record date will, subject to applicable laws, be entitled to instruct the depositary to vote the underlying ordinary shares. The depositary will also determine and inform you of the manner for you to give your voting instructions, including instructions to give discretionary proxies to a person designated by us. Upon receipt of voting instructions of a holder of ADSs, the depositary will endeavor to vote the underlying ordinary shares in accordance with these instructions. You may not receive sufficient notice of a shareholders’ meeting for you to withdraw your ordinary shares and cast your vote with respect to any proposed resolution, as a holder of our ordinary shares. In addition, the depositary and its agents may not be able to send materials relating to the meeting and voting instruction forms to you, or to carry out your voting instructions, in a timely manner. We cannot assure you that you will receive the voting materials in time to ensure that you can instruct the depositary to vote your shares. The additional time required for the depositary to receive from us and distribute to you meeting notices and materials, and for you to give voting instructions to the depositary with respect to the underlying ordinary shares, will result in your having less time to consider meeting notices and materials than holders of ordinary shares who receive such notices and materials directly from us and who vote their ordinary shares directly. If you have given your voting instructions to the depositary and subsequently decide to change those instructions, you may not be able to do so in time for the depositary to vote in accordance with your revised instructions. The depositary and its agents will not be responsible for any failure to carry out any instructions to vote, for the manner in which any vote is cast or for the effect of any such vote. In the event that voting on any resolution or matter is conducted on a show of hands basis in accordance with our second amended and restated memorandum of association and articles of association, the depositary will refrain from voting and the voting instructions (or the deemed voting instructions, as set out in the deposit agreement) received by the depositary from you will lapse. The depositary will have no obligation to demand voting on a poll basis with respect to any resolution and will have no liability to any holder of ADS for not having demanded voting on a poll basis. In addition, the depositary will, if so requested in writing by us, represent all the ordinary shares (whether or not voting instructions have been received in respect of such ordinary shares from you as of the record date) for the purpose of establishing quorum at a meeting of shareholders.

***Except in limited circumstances, the depositary for our ADSs will give us a discretionary proxy to vote our ordinary shares underlying your ADSs if you do not vote at shareholders' meetings, which could adversely affect your interests.***

Under the deposit agreement for the ADSs, the depositary will give us a discretionary proxy to vote our ordinary shares underlying your ADSs at shareholders' meetings if you do not vote, do not timely vote, or voting instructions received fail to specify the manner in which the depositary is to vote ordinary shares underlying your ADSs unless we notify the depositary that:

- we do not wish to receive a discretionary proxy;
- we think there is substantial shareholder opposition to the particular question; or
- we think the subject of the particular question would have a material adverse impact on our shareholders.

The effect of this discretionary proxy is that, absent the situations described above, you cannot prevent our ordinary shares underlying your ADSs from being voted and it may make it more difficult for shareholders to influence the management of our company. Holders of our ordinary shares are not subject to this discretionary proxy.

***We may 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 ordinary shares.***

Depending upon the value of our ADSs or ordinary shares and the nature of our assets and income over time, we could be classified as a passive foreign investment company, or PFIC, for U.S. federal income tax purposes. We will be classified as a PFIC in any taxable year if either (a) the average quarterly value of our gross assets that produce passive income or are held for the production of passive income is at least 50% of the average quarterly value of our total gross assets or (b) 75% or more of our gross income for the taxable year is passive income. According to these technical rules, we would likely become a PFIC for a given taxable year if our market capitalization were to decrease significantly while we hold substantial cash and cash equivalents in that year.

We believe we were not a passive foreign investment company, or PFIC, for U.S. federal income tax purposes for our taxable year ended September 30, 2011. However, the application of the PFIC rules is subject to ambiguity in several respects, and, in addition, PFIC status is tested each taxable year and will depend on the composition of our assets and income and the value of our assets (including, among others, goodwill and equity investments in less than 25% owned entities) from time to time. Because we currently hold, and expect to continue to hold, a substantial amount of cash and other passive assets and, because the value of our assets is likely to be determined in large part by reference to the market prices of our ADSs and ordinary shares, which is likely to fluctuate, there can be no assurance that we will not be a PFIC in the current taxable year or in any future taxable year. If we are treated as a PFIC for any taxable year during which a U.S. investor held our ADSs or ordinary shares, certain adverse U.S. federal income tax consequences would apply to the U.S. investor. For more information on the U.S. tax consequences to you that would result from our classification as a PFIC, please see "Item 10.E. Additional Information — Taxation — United States Federal Income Taxation — Passive Foreign Investment Company."

***Your right to participate in any future rights offerings may be limited, which may cause dilution to your holdings.***

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. However, we cannot make rights available to you in the United States unless we register the rights and the securities to which the rights relate under the Securities Act or an exemption from the registration requirements is available. 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, you may be unable to participate in our rights offerings and may experience dilution in your holdings.

***You may not receive distributions on our ordinary shares or any value for them if such distribution is illegal or if any required government approval cannot be obtained in order to make such distribution available to you.***

The depositary of our ADSs has agreed to pay holders of our ADSs the cash dividends or other distributions it or the custodian for our ADSs receives on our ordinary shares or other deposited securities after deducting its fees and expenses. Holder of our ADSs will receive these distributions in proportion to the number of our ordinary shares such holder's ADSs represent. However, the depositary is not responsible to make a distribution available to any holders of ADSs if it decides that it is unlawful to make such distribution. For example, it would be unlawful to make a distribution to a holder of ADSs if it consisted of securities that required registration under the Securities Act but that were not properly registered or distributed pursuant to an applicable exemption from registration. The depositary is not responsible for making a distribution available to any holders of ADSs if any government approval or registration required for such distribution cannot be obtained after reasonable efforts made by the depositary. We have no obligation to take any other action to permit the distribution of our ADSs, ordinary shares, rights or anything else to holders of our ADSs. This means that holders of our ADSs may not receive the distributions we make on our ordinary shares or any value for them if it is unlawful or unreasonable from a regulatory perspective for us to make them available to such holders. These restrictions may have a material adverse effect on the value of our ADSs.

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

ADSs are transferable on the books of the depository. However, the depository may close its books at any time or from time to time when it deems expedient in connection with the performance of its duties. The depository may close its books from time to time for a number of reasons, including in connection with corporate events such as a rights offering, during which time the depository needs to maintain an exact number of ADS holders on its books for a specified period. The depository may also close its books in emergencies, and on weekends and public holidays. The depository may refuse to deliver, transfer or register transfers of our ADSs generally when the books of the depository are closed, or at any time if we or the depository thinks it is necessary or advisable to do so because of any requirement of law or any government or government body, or under any provision of the deposit agreement, or for any other reason.

***We are a Cayman Islands company and, because judicial precedent regarding the rights of shareholders is more limited under Cayman Islands law than under U.S. federal or state laws, holders of ADSs may have less protection of shareholder rights than they would under U.S. federal or state laws.***

Our corporate affairs are governed by our second amended and restated memorandum of association and articles of association, the Cayman Islands Companies Law (as amended) and the common law of the Cayman Islands. The rights of shareholders to take action against the 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 law than the United States. In addition, some jurisdictions, such as Delaware, have more fully developed and judicially interpreted bodies of corporate law than the Cayman Islands. As a result of all of the above, public shareholders may have more difficulty in protecting their interests in the face of actions taken by management, members of the board of directors or controlling shareholders than they would as public shareholders of a U.S. company, and Cayman Islands companies may not have standing to initiate a shareholder derivative action before the federal courts of the United States.

***Certain judgments obtained against us by our shareholders may not be enforceable.***

We are a Cayman Islands company and substantially all of our assets are located outside of the United States. Nearly all of our current operations are conducted in China. In addition, most of our directors and 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 to effect service of process within the United States upon these persons. It may also be difficult to enforce in U.S. court 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 residents of countries other than 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 China would recognize or enforce judgments of U.S. courts against us or such persons predicated upon the civil liability provisions of the securities laws of the United States or any state. In addition, there is uncertainty as to whether such Cayman Islands or PRC courts would be competent to hear original actions brought in the Cayman Islands or China against us or such persons predicated upon the securities laws of the United States or any state.

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

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

Beijing Champion Hi-Tech Co., Ltd., or Beijing Champion, a PRC limited liability company, commenced operations in July 2000 and became our consolidated operating company in June 2003.

In March 2003, we incorporated China Distance Education Limited, or CDEL Hong Kong, in Hong Kong. We then conducted a series of transactions to reorganize our corporate structure and have CDEL Hong Kong become our offshore holding company.

We incorporated China Distance Education Holdings Limited, or CDEL Cayman, in the Cayman Islands in January 2008 as our listing vehicle. CDEL Cayman became our ultimate holding company in March 2008 when it issued shares to the existing shareholders of CDEL Hong Kong in exchange for all of the outstanding shares of CDEL Hong Kong at a rate of 1,000 shares in CDEL Cayman in return for each share in CDEL Hong Kong.

In March 2009, we acquired the business start-up training services from Beijing Yinglun Yucai Education Consulting Co., Ltd., or Yinglun Yucai, which was owned by Mr. Liang Ma, a third-party individual. The acquired business is operated by Zhengbao Yucai, an entity established by Beijing Champion. With an initial consideration of RMB36.0 million (\$5.3 million), we are entitled to 60% of the ownership interest of Zhengbao Yucai. In January 2010, we sought through arbitration to require Mr. Liang Ma, Yinglun Yucai, and Global Education Consortium Group Co., Limited, to compensate us for the loss incurred as a result of their failure to perform the related agreement. In June 2011, China International Economic and Trade Arbitration Commission, or CIETAC, ruled, among other things, that Mr. Liang Ma shall surrender his 40% ownership interest in Zhengbao Yucai to us for no consideration. For more information with respect to this acquisition, please see “Item 8. Financial Information-Legal Proceedings.”

In September 2009, we acquired the business of Gaokao retake preparation and high-school supplementary tutoring services from Mr. Junnan Ye and Mr. Xiujie Hu, two third-party individuals. The acquired business is operated by Champion Xinlixiang, an entity established by Champion Wangge. With an initial consideration of RMB16.0 million (\$2.4 million), we were entitled to 60% of the ownership interest of Champion Xinlixiang. In November 2010, we agreed with Mr. Junnan Ye and Mr. Xiujie Hu that the profit target for the fiscal year 2010 stipulated in the original purchase agreement was not met by Champion Xinlixiang. Accordingly, pursuant to the terms of the original purchase agreement, Mr. Junnan Ye and Mr. Xiujie Hu surrendered their 40% ownership interest in Champion Xinlixiang to us for no consideration on October 1, 2010. However, with respect to our Gaokao retake preparation and high-school supplementary tutoring business, we have suffered significant operating losses for the fiscal year ended September 30, 2011. As a result, on September 27, 2011, we decided to discontinue such business and put the related assets and business up for sale.

In February 2010, Practice Enterprises Network China International Links Limited, or PENCIL was incorporated in Hong Kong as a wholly-owned subsidiary of CDEL Hong Kong. PENCIL has not conducted any substantive operations since its inception.

We incurred capital expenditures of \$2.6 million, \$1.8 million and \$5.5 million in the fiscal years ended September 30, 2011, 2010 and 2009, respectively. The amount of capital expenditures in the fiscal year ended September 30, 2011 related primarily to our expenditures on property, plant and equipment, and software. These capital expenditures were funded from our operating cash flow. For additional information on our capital expenditures, see Item “5.B. Operating and Financial Review and Prospects – Liquidity and Capital Resources – Capital Expenditures.”

For additional information on our organizational structure, see “Item 4.C. Information on the Company — Organizational Structure.”

Our principal executive offices are located at 18th Floor, Xueyuan International Tower, 1 Zhichun Road, Haidian District, Beijing 100083, the People’s Republic of China. Our telephone number at this address is +86-10-8231-9999 and our fax number is +86-10-8233-7887. Our main website is [www.cdeledu.com](http://www.cdeledu.com). The information contained on this website and our other websites is not part of this annual report.

Our ADSs are listed on the NYSE, under the symbol “DL.” Our agent for service of process in the United States is CT Corporation System, located at 111 Eighth Avenue, New York, New York 10011.

## **B. Business overview**

### **Overview**

We offer a wide range of online education and test preparation courses and other related services and products. Our online courses are designed to help professionals and other course participants obtain and maintain the skills, licenses and certifications necessary to pursue careers in China in the areas of accounting, law, healthcare, construction engineering and other industries. We believe that we are the largest provider of online education in China focusing on professional education, as measured by total number of course enrollments. We also offer online test preparation courses to self-taught learners pursuing higher education diplomas or degrees and to secondary school and college students preparing for various academic and entrance exams. In addition, we offer online foreign language courses. Our online courses feature audio-video lectures delivered through the Internet using streaming media and other Internet-based technologies, and are supplemented by our proprietary textbooks, tutoring, online assignments and exercises, mock examinations and other forms of course-related support. Course participants are able to access our courses through the Internet at times and places most convenient for them and to easily interact with a broad online community of course participants, professionals, lecturers and tutors. In addition, we also offer offline primary and secondary school supplementary courses and offline business start-up training courses.

We launched our first online education course in March 2001 through our [www.chinaacc.com](http://www.chinaacc.com) website to offer online accounting courses designed to help course participants prepare for China's Intermediate Level Accounting Professional Qualification Examination. Our online accounting education business has experienced substantial growth since then. We believe our "Chinaacc" brand has now become widely recognized in China as a leading source for online training, test preparation and continuing education within China's accounting industry. We have also expanded our online course offerings into other areas. In June 2003, we launched a website to provide preparatory courses for China's primary legal exam, the National Judicial Examination. In January 2005, we launched a website to provide training and licensure exam courses for various healthcare professionals, including doctors, nurses and pharmacists. As of September 30, 2011, we operated 17 websites, including our main website [www.cdeledu.com](http://www.cdeledu.com) and 16 other websites, each dedicated to a specific industry, profession or subject area.

In addition to our online education courses, which accounted for 74.0%, 73.6% (adjusted) and 74.1% of our net revenues in the fiscal years ended September 30, 2009, 2010 and 2011, respectively, we also sell books and reference materials through third-party bookstores and distributors across China, and, to a lesser extent, through our online bookstore and our offices in Beijing. In addition, we also further expanded our course offerings into offline areas, including offline primary and secondary school supplementary courses, Gaokao retake preparation and high-school supplementary tutoring business, and business start-up training courses. We also, from time to time, provide course production services, platform production services and magazine content production services for certain customers at their request and provide in-person accounting and healthcare professional training to accounting firms and the general public.

Our net revenues were \$30.1 million, \$32.6 million (adjusted) and \$41.6 million in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. Our net income was \$1.2 million in the fiscal year ended September 30, 2009, and we incurred a net loss of \$1.9 million and \$3.8 million in the fiscal years ended September 30, 2010 and 2011, respectively. Our net loss during the fiscal year ended September 30, 2010 compared to the net income in the fiscal year ended September 30, 2009 resulted mainly from additional share-based compensation expenses arising from our share options granted in the first quarter of the fiscal year ended September 30, 2010, impairment of goodwill, intangible assets and purchased call options acquired with the acquisitions of Zhengbao Yucai and Champion Xinlixiang, and significant bad debts provision arising in that period. We incurred a net loss of \$3.8 million in the fiscal year ended September 30, 2011 mainly due to share-based compensation expenses arising from the re-pricing and acceleration of the vesting of our share options granted under the Prior Plan in the fourth quarter of the fiscal year ended September 30, 2011, and impairment of goodwill, property, plant and equipment, intangible assets and purchased call options acquired with the acquisitions of Zhengbao Yucai and Champion Xinlixiang. Our total course enrollments increased from approximately 1,134,000 for the fiscal year ended September 30, 2009 to 1,215,000 and 1,601,000 for the fiscal years ended September 30, 2010 and 2011, respectively.

### Our Online Education Services

We offer online courses through our websites designed to help course participants obtain and maintain the skills, licenses and certifications necessary to pursue their careers and professions in China. Our online professional education courses cover a wide range of industries, including accounting, law, healthcare, construction engineering and others. We also offer online test preparation courses to self-taught learners pursuing higher education diplomas or degrees and to secondary school and college students for various academic and entrance exams. Additionally, we offer online foreign language courses.

The following table provides data regarding our current online course offerings and classes as of September 30, 2011. Each course typically represents a major examination or continuing education program within an industry or academic field. Our course offerings are comprised of multiple courses and different types of classes within each course.

<u>Subject Area</u>	<u>Website</u>	<u>Number of Course Offerings</u>	<u>Number of Classes</u>
Accounting	<a href="http://www.chinaacc.com">www.chinaacc.com</a>	19	880
	<a href="http://www.ck100.com">www.ck100.com</a>	5	86
Law	<a href="http://www.chinalawedu.com">www.chinalawedu.com</a>	4	160
Healthcare	<a href="http://www.med66.com">www.med66.com</a>	30	825
Construction Engineering	<a href="http://www.jianshe99.com">www.jianshe99.com</a>	17	291
Information Technology	<a href="http://www.itatedu.com">www.itatedu.com</a>	15	46
Occupational Skills Exams	<a href="http://www.chinatat.com">www.chinatat.com</a>	16	144
Higher Education for Self-Taught Learners	<a href="http://www.zikao365.com">www.zikao365.com</a>	56	372
Adult Higher Education	<a href="http://www.chengkao365.com">www.chengkao365.com</a>	2	22
Graduate School Entrance Exams	<a href="http://www.cnedu.cn">www.cnedu.cn</a>	3	82
Foreign Languages	<a href="http://www.for68.com">www.for68.com</a>	24	103
Primary and Secondary Schools	<a href="http://www.ehappystudy.com">www.ehappystudy.com</a>	16	189
	<a href="http://www.g12e.com">www.g12e.com</a>		
<b>Total</b>		<b>207</b>	<b>3,200</b>



Our courses feature audio-video lectures by experienced lecturers or practitioners within their respective fields delivered through a multimedia and interactive web interface using streaming media and other Internet-based technologies. Our online lectures are supplemented by our proprietary textbooks, tutoring, online assignments, exercises, mock examinations and other forms of course-related support.

Visitors to our websites can set up their own registered accounts free of charge. Once they enroll in our courses, course participants may access and view the lectures as often as they choose, which enables them to learn and review the materials at their own pace. Typically, course participants are able to choose among several different lecturers within each course.

To begin each class, course participants log into their online registered accounts to access the course lectures. For each lecture, the web page is divided into separate windows, including the video window, the hyperlink window, and the lecture script window. Through the video screen, course participants can view the video image of the lecturer and hear his or her voice, helping to replicate a classroom-like experience. From time to time during the lecture, the video screen displays the lecturer's handwritten notes, helping to simulate a blackboard effect.

The web page provides hyperlinks allowing course participants to access other useful functions during the lecture. For example, course participants may pause the video at any time to post a question on the question and answer board, to perform an exercise or practice a real exam question and receive a score instantaneously, or to access the bulletin board or other useful links such as a calculator, chat room, reference materials or help information. The lecture script area is where course scripts are displayed, including main exam points, sample questions, explanations, handwritten notes, links to historical exam questions and answers to sample questions posted by course participants.

We also provide our course lectures in the form of downloadable media files that allow course participants to save copies of the lectures onto their own personal computers and to play them offline. We utilize digital rights management, or DRM, technology to restrict the transfer and viewing of our downloadable media files. To accommodate different levels of Internet access and bandwidth available to course participants across China, we provide our course lectures in a number of formats.

To further enhance the learning experience, we maintain a staff of tutors knowledgeable about specific course topics and exams. Course participants can post questions online through our websites and receive replies to their specific questions from our team of tutors, usually within 24 hours after a question is submitted. We provide tutorial sessions, which allow course participants to interact with their lecturers and other course participants using their personal computers. We also host numerous bulletin board discussions within some of our websites that allow course participants to discuss their course work and share feedback with their peers in an interactive online format. Our online bulletin boards also provide us with a valuable means of tracking feedback about our courses, lecturers and services, allowing us to make adjustments and quickly react to concerns and complaints of our course participants.

## ***Our Professional Course Offerings***

### ***Accounting Courses***

PRC laws and regulations require persons engaging in accounting and related activities to obtain various qualifications and licenses, and to meet continuing education requirements. These qualifications and licenses are primarily obtained by passing exams administered by various governmental agencies. Continuing education requirements can be fulfilled by taking courses covering certain continuing education subjects. Through our [www.chinaacc.com](http://www.chinaacc.com) website launched in 2001, we provide a comprehensive body of online preparatory courses designed to prepare course participants primarily for the following professional accounting examinations or to meet certain continuing education requirements.

- ***Accounting Professional Qualification Examination.*** Persons who are engaged in performing PRC accounting work in any organization in China are required to hold a certificate of accounting professional and to register with the relevant regional bureaus of the Ministry of Finance, or the MOF. This is the basic qualification requirement for accounting professionals in China.
- ***Elementary, Intermediate and Advanced Level Accounting Professional Qualification Examinations.*** The skill level and technical competence of accounting professionals in China are further measured by achieving certification at various levels within the profession. These levels are determined by the ability of accounting professionals to pass elementary, intermediate and advanced level accounting professional qualification examinations. Candidates who pass the exam are issued an accounting qualification certificate for their respective level from the MOF and the Ministry of Human Resources and Social Security, or the MOP, jointly.
- ***CPA Qualification Examination.*** Passing China's CPA Qualification Examination is required for persons to act as certified public accountants in China. This exam is open to all candidates who hold at least an associate diploma or an intermediate level of accounting-related professional qualification certificate.
- ***Registered Tax Agent Qualification Examination.*** Under PRC regulations, only registered tax agents are qualified to carry out tax agency services, issue tax audit reports and handle tax procedures such as applications for tax registration with relevant authorities on behalf of business entities. Persons wishing to qualify as registered tax agents must pass the Registered Tax Agent Qualification Examination.

- *Certified Asset Appraiser Examination.* Under PRC regulations, only certified asset appraisers are qualified to carry out legally required valuations of state-owned assets, valuations of non-state-owned assets and valuation consultancy and other valuation-related services. Persons wishing to qualify as certified asset appraisers must pass the Certified Asset Appraiser Examination.
- *Continuing Education for Accounting Personnel.* PRC regulations require persons holding Certificates of Accounting Professional and Certificates of Accounting Specialty and Technical Qualifications to meet the requirements of receiving a minimum number of 24 hours of continuing education training each year. Failure to comply with these continuing education requirements can result in the suspension or cancellation of such certificate holders' certifications.

In November 2009, we entered into an agreement with Becker Professional Education, a subsidiary of DeVry Inc. and a global leader in professional education, under which agreement we obtained exclusive rights to distribute Becker Professional Education's CPA Review and CPA Final Review courses and related materials, for both online and in-person courses, in China.

#### *Legal Courses*

In June 2003, we launched our [www.chinalawedu.com](http://www.chinalawedu.com) website to provide preparatory courses for legal examinations in China. Currently, we offer courses relating to China's most important nationwide legal examination, the National Judicial Examination, which was introduced in 2002 and is administered annually in September by the PRC Ministry of Justice. Persons seeking to become judges, procurators and lawyers in China are required to pass the exam to obtain the legal practitioner qualification certificate. Approximately 410,000, 395,000 and 415,000 candidates sat for the exams in 2009, 2010 and 2011, respectively. We also offer courses for the Enterprise Legal Counsel Examination held annually by the MOP in October for persons wishing to obtain a qualification certificate for in-house legal counsel positions.

#### *Healthcare Courses*

In January 2005, we launched our [www.med66.com](http://www.med66.com) website to provide preparatory courses for a wide variety of healthcare professional exams. Currently, we offer courses mainly relating to three major nationwide healthcare exams: (i) the National Practicing Medical Doctor Qualification Examination, which is organized and administered annually by the Ministry of Health with approximately 800,000 candidates taking the exam in 2011, (ii) the Healthcare Professional Technical Qualification Examination jointly administered by the Ministry of Health and the MOP and (iii) the National Pharmacist Qualification Examination administered by the MOP and the State Administration of Drug Supervision.

#### *Construction Engineering Courses*

In June 2005, we launched our [www.jianshe99.com](http://www.jianshe99.com) website to provide test preparatory courses for construction engineering professionals in China. Currently we offer courses mainly relating to the following exams: Associate Constructor and Constructor Qualification Examinations, Construction Supervisor Qualification Examination, Construction Pricing Engineer Qualification Examination and Certified Safety Engineer Qualification Examination. These examinations are jointly administered by the Ministry of Housing and Urban-Rural Development and MOP.

In addition, we also offer online continuing education courses to construction engineering professionals, including architects, cost estimators, equipment supervisors, real estate appraisers, and realtor associates to help them meet government requirements and maintain their qualifications.

#### *Other Professional Education Courses*

In addition, we also provide professional education courses in the areas of information technology, securities and various civil service positions. Each of these offerings follows a similar course creation and online delivery model. We plan to continue to leverage our core online course creation and delivery expertise to create and deliver new courses for additional professions and industries.

#### *Our Higher Education for Self-Taught Learners*

Through our website [www.zikao365.com](http://www.zikao365.com), we offer courses targeted at self-taught learners pursuing associate diplomas or bachelor's degrees in various academic areas. They complete their self study and obtain government accredited diplomas or degrees by passing the Higher Education Examination for Self-Taught Learners administered by the MOE without having to enroll in and physically attend a traditional college or university. Statistics published by the MOE show that there are approximately 10 million exam takers of Higher Education Examination for Self-Taught Learners each year. We offer test preparatory courses to help self-taught learners pass the requisite exams. We have also entered into multiple-year cooperative agreements, sometimes exclusive, with the respective designated administrator of self-taught study process monitoring programs for self-taught learners in eight provinces and cities to allow self-taught learners to earn up to 30% of the credits they need to obtain associate diplomas or bachelor's degrees.

### ***Our Academic Exam Preparation and Foreign Language Courses Study Courses***

Through our [www.cnedu.cn](http://www.cnedu.cn) website, we offer test preparation courses targeted at university students intending to take nationwide graduate school entrance exams in various disciplines administered by the MOE. Over the past three years, approximately 1.4 million people each year have taken such exams.

We also operate websites focused on the secondary and college education market, foreign language study and other subjects. China's educational system places heavy emphasis on attending good secondary schools as a way to improve course participants' chances of attending more prestigious universities in China. Scoring well on exams at each stage of a secondary school student's educational career is important to improve his or her chances of attending a better university. Our secondary education courses are designed to provide an online resource for secondary school course participants to prepare for these exams.

In September 2010, we entered into an agreement with AsknLearn Pte. Ltd., a subsidiary of Educomp Solutions, India's largest education company, under which agreement we obtained exclusive rights to distribute Educomp's Smart Class®, Edulearn and Wizlearn products in China. Educomp's Smart Class®, Edulearn and Wizlearn products provide dynamic multimedia learning, teaching and administrative content and tools aimed at improving teacher effectiveness and productivity in-class, improving academic performance of students, and effectively managing school administrative processes. The solutions are primarily aimed at the primary and secondary school markets. We have not generated material revenue from these solutions yet. However, we expect them to bolster our primary and secondary school offerings in the future. As part of the agreement, we will provide students and schools in China with access to Smart Class®, Edulearn and Wizlearn via our online platform.

### ***Other Products and Services***

#### ***Books and Reference Materials***

We sell books and reference materials relating to various professional courses and exam subjects. To promote the use of our online courses, we also sell proprietary books and reference materials related to our courses such as the Elementary Level and Intermediate Level Accounting Professional Qualification Examination, the CPA Qualification Examination, the Registered Tax Agent Qualification Examination, Accounting Professional Qualification Examination, accounting continuing education, the National Judicial Examination, the National Practicing Medical Doctor Qualification Examination, the Construction Supervisor Qualification Examination, and the Intermediate Economist Qualification Examination. As we expand our course offerings, we may sell other books and reference materials. To promote our online courses, we sometimes sell books and reference materials together with study cards, which allow customers to take a certain number of on-line courses for no additional charge. Our proprietary guidebooks are authored by lecturers teaching the relevant online courses. In substantially all cases, we own the copyright to these books pursuant to agreements with the lecturers. We engage third-party publishers to publish our reference books. We distribute these books and materials through third-party bookstores and distributors across China, as well as through our online bookstore and our offices in Beijing.

#### ***Offline education services***

##### ***Business Start-up Training Courses***

In March 2009, we acquired the business start-up training business from Yinglun Yucai which was previously owned by Mr. Liang Ma, an independent third party. The training offering targets university students, job seekers and individuals who are interested in learning how to establish new businesses. Such practical training is strongly encouraged by the Chinese government to promote employment opportunities in the country. For this course offering, we prepare training materials in accordance with requirements of the relevant government authorities in various provinces and cities. We do not charge the course participants fees. Instead, we receive subsidies from the relevant government authorities in various provinces and cities, which are conditioned on our ability to meet government stipulated conditions under the subsidy policies. When determining our entitlement to the subsidy, the government authorities consider the passage rate of our course participants' business proposals as evaluated by such authorities, as well as the business start-up rate and employment rate of our course participants.

##### ***Primary and Secondary School Supplementary Courses***

We provide primary and secondary school supplementary tutoring services to students in a range of subject areas, such as Chinese, math and science. Students may attend offline courses taught by our in-person lecturers or view pre-recorded video courses on our website at [www.g12e.com](http://www.g12e.com). Our offline classes are available in Beijing and are most subscribed during winter and summer breaks.

##### ***Accounting and Healthcare Professional Training Courses***

From time to time, we provide in-person professional training for accounting firms. Starting from fiscal year ended September 30, 2011, we also provide in-person accounting and healthcare professional training to the public to further expand our course offerings.

### *Other Services*

#### *Course Production Services*

We provide course production services to certain customers on a contractual basis. We typically create and produce course packages in digital format based on the content requirements of our offline educational institute or company customers.

#### *Platform Production Services*

From time to time, we develop online platforms for our customers and provide them with technical support and maintenance services on a contractual basis. The online platforms enable customers to sell products through our website. After the development of online platforms, we provide after-sale support and maintenance services, which encompass bug fixes and general technical support but do not include upgrades or increased functionality of the online platform, for a limited time at no extra charge.

### *Others*

In April 2011, TStudy Co., Ltd., an integrated education technology company and an affiliate of Time Education, one of the largest private education companies in Korea, granted us the exclusive distribution right for its proprietary digital educational products and software, including Symphony, TStudy Interactive Whiteboard, Dotnote and Tnote in China's public education market. Symphony is a fully interactive classroom solution comprising of digital pens and proprietary software. Dotnote is a personal lecture making, note management, and homework management program primarily utilizing TStudy digital pens, a unique new technology which digitally transcribes notes taken on specialized dot pattern paper notebooks. Tnote is an online based distance learning solution comprising of digital pens and a comprehensive online learning management system which enables teachers to fully interact with students online. TStudy's products are important additions to our suite of solutions for the primary and secondary school education business line. TStudy's products, coupled with EduComp's Smart-Class content and online content that we developed for our "Famous School Coalition" initiative, will provide us with a comprehensive and powerful platform and content offering at the primary and secondary school market.

From time to time, we also provide accounting magazine content production services to certain customers on a contractual basis.

#### ***Discontinued Operation - Gaokao Retake Preparation and High-School Supplementary Tutoring Services***

In September 2009, we acquired the business of Gaokao retake preparation and high-school supplementary tutoring services that were previously established and operated by Mr. Junnan Ye and Mr. Xiujie Hu, two independent third parties. With respect to such business, we had suffered significant operating losses for the fiscal year ended September 30, 2011. As a result, we decided to discontinue such business and put the related assets and business up for sale. For more information, please see "Item 5. Operating and Financial Review and Prospects."

### **Our Regular, Premium and Elite Classes**

We offer regular, premium and elite classes. Our regular, premium and elite classes are mainly comprised of the following four types:

- *Foundation Classes:* Our foundation classes contain detailed instructions and content to provide course participants with a broad and comprehensive knowledge base relating to a specific subject area.
- *Intensified Focus Classes:* Our intensified focus classes are designed to provide more intensive instructions focused on important topics in a specific subject area at a more advanced pace to course participants who already have basic knowledge of the subject area.
- *Exam Questions Analysis Classes:* Our exam questions analysis classes contain materials and instructions tailored specifically to preparation for the actual exams and the types of questions and topics that come up on each exam.
- *Crash-Course Classes:* Our crash-course classes are designed to provide a quick review of critical topic areas for specific exam subjects to enable course participants to make final preparations in the weeks prior to an exam.

In November 2006, we introduced elite classes for some of our most popular accounting courses, such as courses for the Elementary Level and Intermediate Level Accounting Professional Qualification Examination, the CPA Qualification Examination and the Registered Tax Agent Qualification Examination. We also offer elite classes to legal practitioners, self-taught learners pursuing higher education diplomas or degrees, and professionals in the healthcare, construction engineering and other industries. With our elite classes, course participants pay substantially higher course fees for more personal and tailored course-related services. After completing an elite class, if a participant fails to pass the exam for that subject, and certain pre-agreed conditions are met, the course participant is entitled to a refund of the applicable course fees paid or the course participant can choose to use such amounts to register and pay for future courses provided by us.

In exchange for higher course fees, our elite class participants enjoy high-quality elite course-related support services. Leveraging the technological features available to online course delivery, elite classes allow substantially more interactive and multi-faceted course participation. For example, during a lecture, when a key knowledge point has reached, the lecture automatically pauses and a quiz relating to the point will pop up on the screen. The lecture will not proceed to the next topic until the course participant has correctly responded to the question. This feature ensures that course participants do not miss any of the important knowledge points that may be tested on exams. We believe that these types of interactive features, made possible by the flexibility of our online format, offer distinct advantages over traditional classroom course delivery as well as traditional online teaching methods.

Elite class participants also enjoy personalized support and services provided by our course support service staff. Some of our most experienced tutors work closely with elite class participants and provide them with more individually tailored support and services. For example, questions raised by elite class participants are responded to by tutors on a priority and expedited basis. In addition, a regular study monitoring report is generated by our course support service staff for each elite class participant to ensure that he or she is making satisfactory progress in the course.

Our premium classes represent another course model we introduced in August 2008 for some of our most popular courses, such as courses for the accounting, legal and healthcare industries. To date, we also offer premium classes to self-taught learners pursuing higher education diplomas or degrees, and professionals in the construction engineering and other industries. Our premium class participants enjoy high-quality premium course-related support services similar to the elite class participants. However, premium course participants do not enjoy refund privileges. Instead, in general, if a participant fails to pass the course examination and certain pre-agreed conditions are met, the course participant can retake the same premium course and pay only 50% of the course fees. The participant is given this 50% discount only once, and therefore, if he or she fails the relevant course examination again and wishes to retake the premium course for the third time, there is no discount provided at that time. If a participant fails to pass the course examination for the examinations of American Institute of CPAs and certain healthcare courses, however, the course participant can retake the same courses free of charge for the following year if certain pre-agreed conditions are met.

### **Course Fees and Payment Methods**

We charge course fees on a per-class basis. Course participants may choose to take some or all the classes for each subject offered in each course according to their individual needs. Special package pricing is offered if a participant chooses to take more than one class for a subject in a course. To promote the use of our online courses, we also offer course discounts to eligible course participants who are frequent users of our services. The discounts offered typically range from 20% to 40% off the stated course fees.

Payment for the course fees can be made through any one of the following methods:

- use of our pre-paid study cards;
- remittance through a bank or post office;
- online payment using credit or debit cards via external payment networks; or
- cash payment made at our offices.

Our study cards are pre-paid scratch cards sold through our regional sales agents at points of sale throughout China. The pre-paid study cards come with face values ranging from RMB10 (\$1.6) to RMB1,000 (\$156.8). Course participants may purchase and use these study cards to register and pay for our courses. We first introduced pre-paid study cards in January 2003. In 2006, we began selling a “One Card Pass,” which can be used for multiple courses. This new card eliminates the need for our regional sales agents to purchase multiple types of cards and also provides an opportunity to cross-sell our course offerings. The One Card Pass comes with face values ranging from RMB10 (\$1.6) to RMB500 (\$78.4). These pre-paid study cards and One Card Pass were sold with expiration dates, typically two to three years from the print dates. In addition to the “One Card Pass,” we have another type of pre-paid study cards, which can be used solely for our accounting continuing education courses and have expiration dates, typically one year from the print dates.

With regard to business start-up training courses, course participants are able to attend free of charge. Instead, we receive a subsidy from government authorities if certain stipulated conditions under the government subsidy policy are met.

### **Online Course Creation**

We place great emphasis on the quality of our courses and learning materials, both in terms of substance and production quality to enhance course participants’ learning experience. Working together with our lecturers in each subject, we internally develop and produce the online lectures for most of our courses. We employ a variety of measures including substantive content review and content approval at various stages of the course development process by our experienced in-house personnel to create high-quality courses.

We believe superior delivery of our courses and learning materials over the Internet is also important to attracting and retaining course participants. We record, digitize and edit most of the audio-video lectures used in our courses on our own premises. We maintain 19 fully-equipped recording rooms to ensure the high-quality of the audio-video content and any graphics used in the lectures. Our editing department uses advanced digital audio-video editing software and equipment to eliminate breaks, pauses and unwanted noises from each lecture tape to further enhance the viewing and listening experience. All lectures are properly formatted to facilitate smooth transmission through our websites using streaming media and other Internet-based technologies. Our customer service team regularly seeks feedback on the quality of our courses from our course participants.

### **Community-oriented Services on Our Websites**

In addition to using our websites to access our courses, course participants and visitors to our websites are also able to access a wide variety of other content and information and to communicate and interact with each other. The breadth and depth of our website content has attracted a large number of visitors and has contributed to the fast growth in the awareness of our brands.

Visitors to our websites have free access to comprehensive and timely information about exam times and locations, test preparation guidance, regulations and policies relevant to each industry, career planning and advancement and industry and market trends. We also offer free trial courses on our websites to prospective course participants who wish to try our courses before making the enrollment decision.

We offer free e-mail accounts to course participants. We also provide electronic bulletin board service forums and access to online chat-rooms. Many of our websites feature a blog page that allows course participants and other visitors to our websites to communicate and share ideas and thoughts about topics of common interest. On any blog we provide, people can write and post articles, create and participate in discussions and gain information and insights on topics of interest within the relevant industry or subject matter.

Through our community-oriented websites, we create virtual communities for course participants and visitors that share a common interest in the topics relating to the various professions and subject areas for which we offer our online courses and related services. We believe our community-oriented websites are a valuable means for creating brand awareness and customer loyalty.

### **Our Lecturers**

Our online course lecturers include academics from renowned higher education institutions in China and experienced practitioners within their respective fields. Our online lecturers work with us to prepare the course content and lectures, while also serving as faculty members of various colleges and universities across China or working in their respective fields. They are not our employees and are typically engaged for a one-to-three year period, except for some more experienced lecturers for whom the contract periods are relatively longer and some of them are obligated to conduct online lectures exclusively for us. The number of online lecturers actively producing online courses for us was 629, 370 and 325 in the fiscal years ended September 30, 2009, 2010 and 2011, respectively.

To ensure the quality of our online lecturers, we have established stringent selection and retention criteria and have implemented ongoing monitoring and evaluation procedures. We seek to engage online lecturers who have a strong command of the respective subject areas and good communication skills. In particular, we seek online lecturers capable of, and preferably experienced in, delivering effective instruction through the audio-video format. Our internal quality control personnel regularly monitor the teaching quality of each online lecturer. We also collect feedback on the online lecturers from our course participants on a regular basis through multiple channels, including calls received by our customer service call center, our online course comment book, our online question and answer board and bulletin board service forum. We provide ongoing training for online lecturers and help them improve their online presentation skills based on this feedback.

Our online lecturers are attracted to our online platform where tens of thousands of course participants across China can listen to and view their lectures. Our innovative lecture delivery model helps our online lecturers further expand and enhance their national reputation in their relevant fields. We pay our lecturers fees in either of two ways: the first and most common way is to pay them based on the number of hours of lectures they deliver, and the second and less common way is a course fee sharing arrangement primarily for some of our newer courses.

Although our online lecturers participate in the creation and development of the course materials, in almost all cases, we own all copyrights to our courses and course materials pursuant to contracts with our online lecturers.

## **Course-Related Support and Services**

We employ a service-oriented approach and devote significant resources to developing course-related support and services for our course participants. We maintain a well-trained pool of tutors, numbering 192 as of September 30, 2011, of which 68 are part-time employees. Our tutors are knowledgeable in the relevant fields and experienced with various types of exams or subject matters. They are able to provide timely and accurate responses, usually within 24 hours after a question is submitted, through our online question and answer board to various course-related questions raised by our course participants. To ensure the accuracy of our responses, we introduced the second reviewer policy by which all responses of our most popular courses have to be reviewed by a senior tutor before they are delivered to our students. To ensure that our tutors are suitably qualified to support our courses, we have established stringent selection criteria and make hiring decisions based on academic qualifications, tutorial experience and knowledge of various exams and subject matters. We require our tutors to possess, at a minimum, a college degree in the relevant academic area or a certification in the relevant industry, as well as familiarity with the actual exam and related subject matter.

We believe that our high-quality tutorial and learning support service is critical to enhancing the learning experience of our course participants. Additionally, it helps us generate customer loyalty and attract potential course participants through recommendations from our existing course participants.

## **General Customer Service and Support**

We have a dedicated general customer service team composed of 174 individuals as of September 30, 2011 that our customers can contact by email, our online customer service system or phone through our dedicated call center, 24 hours a day, seven days a week. Our customer support team members provide potential and existing course participants with comprehensive information and counseling regarding our courses and services, recommend suitable courses based on individual needs, assist in course enrollment, accept course fee payments, conduct regular telephone interviews seeking customer feedback on course participation experience and provide additional technical and other support on how to use and get the most out of our courses. We recruit our customer service personnel from candidates who have good communication skills and are committed to providing quality service to our customers. We provide on-the-job training for our new recruits, which includes pairing new recruits with experienced team members as mentors to train them in taking calls from customers. On an ongoing basis, we also evaluate the performance of our customer service staff, and provide training to improve their skills and inform them on new developments in our business.

## **Sales and Marketing**

We rely on a combination of regional and online sales agents, referrals and cross-selling, as well as other sales and marketing activities to market our services and products.

### ***Regional Sales Agents***

We use regional sales agents to sell our pre-paid study cards, which represent the primary method for us to sell and receive payment for our courses. Our regional sales agents are comprised mostly of stores and other points of sale selling books, learning materials and other supplies to our target industries and professions. These agents sell our study cards and are responsible for promotion and advertising of our services in the regions where they operate. They also provide market feedback, which helps us in planning our marketing strategy and sales activities. As of September 30, 2011, we had approximately 1,400 active regional sales agents throughout China.

When selecting regional sales agents, we consider various criteria, such as whether the candidates have relevant experience, and whether they are familiar with or have established relationships with local professionals, professional associations and organizations related to our target industries and professions. Generally, we provide various discounts to our regional sales agents based on the volume purchased and method of payment. Most of our regional sales agents are appointed on a non-exclusive basis.

We also use regional sales agents to recruit course participants of the primary and secondary school supplementary courses offered by Champion Xinlixiang.

### ***Online Agents***

Our online agents are typically Internet companies and website operators in China that market our course offerings and other services on their websites. We pay our online agents a commission for each new course participant registered through their website. As of September 30, 2011, we had approximately 4,300 online agents marketing our online courses through their websites.

### ***Referrals and Cross-Selling***

Many of our customers learn about our services and courses through word-of-mouth referrals. As a result, many of our customers contact us directly about enrolling in our courses. Accordingly, a significant portion of our sales are made through our customer service team. We believe that combining the customer service and sales function in one department contributes both to the quality of our customer services and the effectiveness of our direct sales. Based on their knowledge of our courses and relevant feedback they gain from addressing the questions and comments of existing or past course participants, our customer service personnel are able to recommend the most suitable courses for new customers. Combining these two functions also allows our customer service team members to cross-sell new or additional courses, learning tools and materials, as appropriate, when they are addressing questions from existing course participants.

### ***Other Advertising and Marketing Efforts***

We place advertisements on high-traffic Chinese Internet portals and television, in newspapers, magazines, journals, cinemas and on buses in many cities across China. We also promote our courses, services and products at examination registration centers, and education and career fairs. To raise our profile and promote our courses, regional sales agents normally assist with our promotional activities in their respective regions.

Our sales and marketing team participates in and conducts information sessions at various educational trade fairs, and distributes promotional materials to potential course participants at various examination registration centers. We further promote our courses by handing out complimentary study cards together with reference books and study materials that we sell at these examination registration centers. We have also established a number of scholarships totaling over RMB0.8 million (\$0.1 million) in the fiscal year ended September 30, 2011 and granted awards to course participants who have achieved outstanding performances in various exams. These activities help to improve our profile and enhance our public image.

### **Online Platform and Technology Infrastructure**

Building a reliable, scalable and secure technology infrastructure is crucial to our ability to support the online courses and services we provide to our customers. We manage our online course creation and delivery system using a combination of commercially available software, hardware systems and proprietary technology. Over the years, we have established a comprehensive and powerful online platform that supports the ability for tens of thousands of course participants to simultaneously attend our courses and participate in other programs and activities online. We have also built a robust online community platform that helps build a strong sense of community among our course participants, which contributes to the brand loyalty of our customers.

We maintain multiple servers, which access the Internet backbone via a 5,130 Mbps broadband line. These servers are separately located in multiple hosting facilities in several cities across China to mitigate any downtime arising from individual server failure. For reliability, availability and serviceability, we have created an environment in which each server can function independently. We regularly back up our databases. Based on cluster technology, our system can identify errors and isolate failed servers automatically so that our customers can access our services at any time. When a malfunction arises in a server or at a point of presence, the load balancing technology adopted by us is able to automatically direct visitors to access the same contents through another server or another point of presence. Our network administration department regularly monitors the performance of our websites and infrastructure to enable us to respond quickly to potential problems. We have not experienced a material disruption to our business or websites.

We utilize streaming media technology as the primary delivery method for our online lectures. Using streaming media technology, an end-user can continuously view the file as it is being delivered. To accommodate different levels of Internet access and bandwidth available to course participants across China, we also allow our course participants to download our audio-video lectures. We utilize DRM technology to restrict the transfer and viewing of our files being downloaded.

### **Competition**

We face competition from providers of traditional offline education and test preparation services in China, and expect to face increasing competition from existing competitors and new market entrants in the online education and test preparation market.

The provision of professional education and test preparation courses over the Internet is a relatively new concept in China. Although it is increasingly perceived as an acceptable means of receiving training and instruction, traditional classroom instruction is still generally perceived as the more accepted method. We therefore compete with traditional in-person educational institutions and training centers in the various areas for which we offer courses.

In addition, due to low barriers to entry for Internet-based businesses, we expect to face increasing competition from existing domestic competitors and new entrants to the online education market. We may face increased competition from international competitors that cooperate with local businesses to provide services based on the foreign partners' technology and experience developed in their home markets. Currently, our online competitors include general information websites that have branches providing online training courses, traditional schools that provide online offerings and newly established online training and test preparation businesses.



With the continuous expansion of our course offerings to offline courses since 2009, we face competition from providers of both traditional offline education and online education in these areas.

We believe that the key competitive factors in our industry include the professional competence of lecturers and tutors, price, quality, market recognition and brand name, customer service and the performance of the technological platform. Some of our present and future competitors may have longer operating histories, larger teams of professional staff and greater financial, technical, marketing and other resources. For a discussion of risks relating to competition, see “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — We may lose market share and our profitability may be materially and adversely affected, if we fail to compete effectively with our present and future competitors or to adjust effectively to changing market conditions and trends.”

### **Intellectual Property**

Our trademarks, copyrights, domain names, trade secrets and other intellectual property rights distinguish our products and services from those of our competitors and contribute to our ability to compete in our target markets. We rely on a combination of copyright and trademark law, trade secret protection and confidentiality agreements with our employees, lecturers, business partners and others, to protect our intellectual property rights. In addition, we require our employees to enter into agreements with us under which they acknowledge that all inventions, trade secrets, works of authorship, developments and other processes made by them during their employment are our property and they should assign the same to us if we so require. We also maintain a dedicated team that regularly monitors any infringement or misappropriation of our intellectual property rights.

We have registered 39 software copyright for our proprietary online course delivery platform, customer service system, DRM encryption system, streaming media load balancing system, online course creation management system and certain other aspects of our online education platform with the National Copyright Administration of the PRC. We have also registered 349 trademarks with the China Trademark Office and an additional 40 trademark applications are currently pending. We, however, cannot assure you that all of our trademark applications will be successful.

As of February 24, 2012, we had registered 230 domain names relating to our business with the Internet Corporation for Assigned Names Numbers and China Internet Network Information Center, including those of all our 17 operating websites.

Our intellectual property is subject to risks of theft and other unauthorized use, and our ability to protect our intellectual property from unauthorized use is limited. In addition, we may be subject to claims that we have infringed the intellectual property rights of others. See “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — Our failure to protect our intellectual property rights may undermine our competitive position, and litigation to protect our intellectual property rights or defend against third-party allegations of infringement may be costly and ineffective.”

### **Seasonality**

We have experienced seasonality and expect in the future to continue to experience seasonality in revenues related to the provision of our education courses primarily due to seasonal changes in course enrollments and the timing of various exams. We typically open new online courses to enrollment approximately six months before the relevant exam date. As the majority of our course participants take non-refundable courses relating to the main professional accounting exams, which are typically held in May and September, we historically have experienced higher revenues during the quarters ending June 30 and September 30 of each fiscal year. With respect to our refundable courses, which is also primarily related to the main professional accounting exams, we typically recognize revenues 15 days after the release of the relevant exam results when the participants’ applicable refund privileges expire, resulting in higher revenues in the quarter ended March 31 and September 30. With respect to our professional continuing education courses, we typically recognize revenues when course participants complete the stipulated study hours and take the examinations, or on a straight line basis over the subscription period, starting from a course participant’s enrollment date, ranging from three months to one year. As the majority of our course participants take accounting professional continuing education courses in the second half of the calendar year, we historically have experienced higher revenues during the quarters ending September 30 and December 31 of each fiscal year. As a result, we historically have generated higher revenue in the second half of each fiscal year. This seasonality factor may change in future periods if the timing of exams changes. In addition, as the mix of types of exams and course subjects changes over time, we expect to continue experiencing seasonality based on the timing of various exams.

### **Regulations**

The provision of our online and offline education services is subject to PRC laws and regulations relating to the telecommunications industry and the education services industry. This section sets forth a summary of the principal laws and regulations that affect our business activities in China, the industries in which we operate, and our shareholders’ right to receive dividends and other distributions from us.

### ***Restrictions on Telecommunications Industry***

The telecommunications industry, including the Internet sector, is highly regulated by the PRC government. Laws and regulations issued or implemented by the State Council, Ministry of Industry and Information, or MII, and other relevant government authorities cover virtually every aspect of telecommunications network operations, including entry into the telecommunications industry, the scope of permissible business activities, interconnection and transmission line arrangements, tariff policy and foreign investment. The principal regulations governing the telecommunications industry and the Internet include:

- The Telecommunications Regulations (2000);
- The Administrative Measures for Telecommunications Business Operating Licenses (2009); and
- The Internet Information Services Administrative Measures (2000).

These regulations categorize all telecommunications businesses in China as either “basic telecommunications businesses” or “value-added telecommunications businesses.”

In addition to the regulations promulgated by the PRC central government, some local governments have also promulgated local rules applicable to Internet companies operating within their respective jurisdictions.

### ***Foreign Ownership Restrictions on Internet Content Provision Businesses***

The State Council promulgated the Administrative Rules on Foreign-Invested Telecommunications Enterprises in December 2001, as amended on September 10, 2008, or the FITE Rules. The FITE Rules set forth detailed requirements with respect to capitalization, investor qualifications and application procedures in connection with the establishment of a foreign-invested telecommunications enterprise. Pursuant to the FITE Rules, the ultimate capital contribution ratio of the foreign investor or investors in a foreign-funded telecommunications enterprise that provides value-added telecommunications services shall not exceed 50%.

In addition, for a foreign investor 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 value-added telecommunications business overseas. Moreover, foreign investors that meet these requirements must obtain approvals from MII and the Ministry of Commerce or their authorized local counterparts, which retain considerable discretion in granting approvals.

On July 26, 2006, MII publicly released the Notice on Strengthening the Administration of Foreign Investment in Operating Value-added Telecommunications Business, dated July 13, 2006, or the MII Notice, which reiterates certain provisions under the FITE Rules. According to the MII Notice, if any foreign investor intends to invest in a Chinese telecommunications business, a foreign-invested telecommunications enterprise shall be established and such enterprise shall apply for the relevant telecommunications business licenses. The MII Notice prohibits domestic telecommunication services providers from leasing, transferring or selling telecommunications business operating licenses to any foreign investor in any form, or providing any resources, sites or facilities to any foreign investor for their illegal operation of a telecommunications business in China. According to the MII Notice, either the holder of a value-added telecommunication service license or its shareholders must directly own the domain names and trademarks used by such license holders in their provision of value-added telecommunication services. The MII Notice also requires each license holder to have the necessary facilities, including servers, for its approved business operations and to maintain such facilities in the regions covered its license. In order to comply with the MII Notice, we have transferred all domain names and trademarks that are used primarily in connection with our online business activities from Champion Technology to Beijing Champion.

As a result of current PRC laws and regulations that impose substantial restrictions on foreign investment in Internet businesses in China, we conduct our online education and test preparation business in China through a series of contractual arrangements entered into among our two PRC subsidiaries, Champion Technology and Champion Education Technology, and our affiliated PRC entity, Beijing Champion, which is a domestic PRC company incorporated in the PRC and owned by Zhengdong Zhu, our chairman and chief executive officer, and Baohong Yin, our co-founder and deputy chairman, both of whom are PRC citizens. These contractual arrangements enable us to exercise effective control over and to receive a substantial portion of the economic benefits from Beijing Champion. Beijing Champion has obtained the licenses and approvals that are required to operate our online education and test preparation business. We do not have any direct ownership interests or direct voting rights in Beijing Champion.

Our contractual arrangements with Beijing Champion include a technical support and consultancy services agreement pursuant to which Champion Technology is entitled to receive service fees from Beijing Champion. In addition, Champion Technology has entered into equity pledge agreements (as amended and restated) with each of the shareholders of Beijing Champion, pursuant to which each shareholder has pledged all of his or her interest in Beijing Champion to Champion Technology as security for the performance of Beijing Champion's obligations under the technical support and consultancy services agreement. Pursuant to an exclusive purchase rights agreement with Beijing Champion and its shareholders, CDEL Hong Kong or any third-party designated by CDEL Hong Kong has the right to acquire, in whole or in part, the equity interest of Beijing Champion, when permitted by applicable PRC laws and regulations. There are also certain other agreements and letters of undertaking under the contractual arrangements. For a detailed discussion of these contractual arrangements, see "Item 4.C. Information on the Company — Organizational Structure."

In the opinion of Jingtian & Gongcheng, our PRC legal counsel:

- the ownership structures of Beijing Champion and its subsidiaries and our wholly owned subsidiaries in China are in compliance with existing published PRC laws and regulations; and
- our contractual arrangements among our wholly owned subsidiaries in China and Beijing Champion and its shareholders, are valid and binding, will not result in any violation of published PRC laws or regulations currently in effect, and are enforceable in accordance with their terms and conditions.

However, there are substantial uncertainties regarding the interpretation and application of PRC laws and regulations, including the laws and regulations governing the enforcement and performance of our contractual arrangements in the event of imposition of statutory liens, bankruptcy and criminal proceedings. Accordingly, we cannot assure you that the PRC regulatory authorities will not ultimately take a contrary view. If the PRC government finds that the agreements that establish the structure of our operations in China do not comply with PRC government restrictions on foreign investment in our industry, we could be subject to severe penalties. In addition, for a detailed description of the risks associated with our corporate structure and these contractual arrangements that support our corporate structure, see "Item 3.D. Key Information — Risk Factors — Risks Relating to Our Corporate Structure and Restrictions on Our Industry."

#### ***Regulations on Value-added Telecommunications Services and Internet Content***

Under PRC laws and regulations, Internet content provision services are classified as value-added telecommunications businesses, and a commercial operator must obtain a Telecommunications and Information Services Operating License, or ICP license, from the appropriate telecommunications authority in order to carry out commercial Internet content provision operations in China. These regulations also provide that if the Internet information services are provided in more than one province, then an inter-provincial ICP license must be obtained from MII, while if only one province is involved, the license can be obtained from the relevant provincial telecommunications administration. In addition, the regulations further provide that operators involved in Internet content provision that operate in sensitive and strategic sectors, including news, publishing and education, must obtain additional approvals from the relevant authorities in charge of those sectors.

Each of Beijing Champion, Caikaowang, Champion Wangge and Zhengbao Yucai holds an ICP license issued by the Beijing Telecommunications Administration Bureau, a local branch of the MII, which allows it to provide Internet content distribution services through 17 websites owned by Beijing Champion and its subsidiaries. The ICP license held by Beijing Champion is valid through August 25, 2013, the ICP license held by Caikaowang is valid through July 10, 2013, the ICP license held by Champion Wangge is valid through November 9, 2014, and the ICP license held by Zhengbao Yucai is valid through May 6, 2015. These licenses and approvals are essential to the operation of our online professional education and test preparation services business.

#### ***Regulation of Internet Content***

The PRC government has promulgated measures relating to Internet content through a number of ministries and agencies, including MII, the Ministry of Culture, the Press Office of the State Council and the State Press and Publications Administration. These measures specifically prohibit Internet activities that result in the publication of any content that is found to, among other things, propagate obscenity, gambling or violence, instigate crimes, undermine public morality or the cultural traditions of China 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. Under these measures, ICP license holders are required to monitor their websites, including chat rooms and electronic bulletin boards, for prohibited content and remove any such content that they discover on their websites.

The posting of news on websites and the distribution of news over the Internet are highly regulated and can only be engaged in by ICP license holders that have been specifically approved to do so. The Provisional Administrative Measures Regarding Internet Websites Carrying on the News Posting Business issued by the Press Office of the State Council and MII in November 2000 provide that only websites that are established by government-authorized news agencies may operate online news posting businesses and post news reported by news agencies. Other general websites not established by news agencies may apply to the State Council News Office for approval to post on their websites news supplied contractually by approved news providers. A copy of the relevant news supply contract must be filed with the applicable provincial information offices where such other websites are located. These regulations also provide specific requirements with respect to facilities and level of experience of personnel that must be met by applicants for approval to post news on their websites. According to the Administration of Internet News Information Services Provisions promulgated by the Press Office of the State Council and MII on September 25, 2005 and effective as of such date, the term “news information” in these provisions means news information about current affairs, including reports and commentaries on social and public affairs such as political, economic, military and foreign affairs, as well as reports and commentaries on sudden social events. The term “Internet news information services,” means publication of news information, provision of electronic bulletin board services for current affairs and distribution of information of current affairs to the public through the Internet. The Press Office of the State Council is in charge of nationwide supervision and regulation of Internet news information services. The press office of each province, autonomous region and municipality directly under the central government is in charge of regulating the Internet news information services within its administrative region. If any information we provide through our websites is deemed current affairs, we may be subject to the above regulations.

### ***Regulation of Broadcasting Audio-Video Programs through the Internet or Other Information Network***

The State Administration of Radio, Film and Television, or SARFT, promulgated the Rules for Administration of Broadcasting of Audio-Video Programs through the Internet and Other Information Networks, or the Broadcasting Rules, in 2004, which became effective on October 11, 2004. The Broadcasting Rules apply to the activities of broadcasting, integrating, transmitting and downloading of audio-video programs with computers, televisions or mobile phones and through various types of information networks. Pursuant to the Broadcasting Rules, a Permit for Broadcasting Audio-Video Programs via Information Network is required to engage in these Internet broadcasting activities. On April 13, 2005, the State Council announced a policy on private investments in businesses in China relating to cultural matters that prohibits private investments in businesses relating to the dissemination of audio-video programs through information networks.

On December 20, 2007, SARFT and MII issued the Internet Audio-Video Program Measures, which became effective on January 31, 2008. Among other things, the Internet Audio-Video Program Measures stipulate that no entities or individuals may provide Internet audio-video program services without a License for Disseminating Audio-Video Programs through Information Network issued by SARFT or its local counterparts or completing the relevant registration with SARFT or its local counterparts and only entities wholly owned or controlled by the PRC government may engage in the production, editing, integration or consolidation, and transfer to the public through the Internet, of audio-video programs, and the provision of audio-video program uploading and transmission services. On February 3, 2008, SARFT and MII jointly held a press conference in response to inquiries related to the Internet Audio-Video Program Measures, during which SARFT and MII officials indicated that providers of audio-video program services established prior to the promulgation date of the Internet Audio-Video Program Measures that do not have any regulatory non-compliance records can re-register with the relevant government authorities to continue their current business operations. After the conference, the two authorities published a press release that confirms the above guidelines. On September 15, 2009, SARFT promulgated a notice regarding the issues of the management of Internet Audio-Video Program Services License, pursuant to which, the closing date of the application for re-registration of the Internet Audio-Video Program Services License was December 20, 2009.

Due to uncertainties with respect to the interpretation and application of the Internet Audio-Video Program Measures, each year, we and our PRC counsel consult the Beijing Branch of SARFT, or Beijing SARFT, which is the competent authority in Beijing to grant the License for Disseminating Audio-Video Programs through Information Network, by way of face-to-face interview or telephone consultation regarding whether online education services providers like us that provide audio-video educational courses and programs through the Internet only to enrolled course participants should apply for said license. The officials in Beijing SARFT replied verbally in 2008, 2009 and early 2010 that we were not required to apply for said license as we are an education service provider that only transmits audio-video educational courses and programs through the Internet to enrolled course participants instead of the general public. However, when we consulted Beijing SARFT again in January 2011, Beijing SARFT indicated that the scope of application of the Internet Audio-Video Program Measures was expanded by SARFT to cover educational course providers like us and thus we are required to apply for the License for Disseminating Audio-Video Programs through Information Network. Further to the application scope expansion, in January 2011, a joint administrative enforcement commission of the Beijing government (including Beijing SARFT) issued a warning to us and fined us RMB6,000 (\$897) for providing audio-video educational courses without obtaining the License for Disseminating Audio-Video Programs through Information Network. After the consultation, we began to apply to Beijing SARFT for said license. After accepting our application in February 2011, Beijing SARFT sent us a written reply on March 8, 2011. According to the reply, due to the special circumstance that we have been involved in the distance education industry for many years and our websites [www.chinaacc.com](http://www.chinaacc.com), [www.chinalawedu.com](http://www.chinalawedu.com), and [www.ck100.com](http://www.ck100.com) had been approved by the Ministry of Education and the related telecommunication authority before the promulgation of Internet Audio-Video Program Measures, Beijing SARFT would further deliberate our application and officially respond to us thereafter. On August 1, 2011, Beijing SARFT sent us another written reply which states that Beijing SARFT had consulted with SARFT and determined that the License for Disseminating Audio-Video Programs through Information Network is not applicable to us as basic education, higher education, teacher education, vocational education, adult education, and distance education activities do not fall under the “Internet audio-visual services program.” Therefore, we are not required to obtain the License for Disseminating Audio-Video Programs. We cannot guarantee that Beijing SARFT will not change its position or that the reply will not be challenged by higher authorities in China, or that we will not be asked to obtain the said license again. If the regulatory authorities take any such actions against us, it may materially and adversely affect our business. Moreover, if we are asked to re-register with relevant authorities or obtain the required license, we cannot assure you that our future application(s) will be approved by relevant authorities in a timely manner or at all. If we are subsequently required to and are unable to re-register or obtain the necessary license timely, or at all, due to reasons beyond our control, our equity ownership structure may require significant restructuring, or we may become subject to significant penalties, fines, legal sanctions or an order to suspend our use of audio-video content, any of which could have a material adverse effect on our business, financial condition, results of operations, and prospects, as well as the trading price of our ADSs.

### ***Regulation of Information Security***

Internet content in China is also regulated and restricted by the PRC government to protect state security. The National People’s Congress has enacted a law that may subject to criminal punishment in China any person who: (i) gains improper entry into a computer or system of strategic importance; (ii) disseminates politically disruptive information; (iii) leaks state secrets; (iv) spreads false commercial information; or (v) infringes intellectual property rights.

The Ministry of Public Security has promulgated measures that prohibit use of the Internet in ways that, among other things, result in a leakage of state secrets or a spread of socially destabilizing content. The Ministry of Public Security has supervision and inspection rights in this regard, and we are 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. We believe we are in compliance with these regulations.

### ***Regulation of Domain Names and Website Names***

PRC law requires owners of Internet domain names to register their domain names with qualified domain name registration agencies approved by MII and obtain registration certificates from such registration agencies. A registered domain name owner has an exclusive use right over its domain name. Unregistered domain names may not receive proper legal protections and may be misappropriated by unauthorized third parties. As of February 24, 2012, we had registered 230 domain names relating to our websites, with the Internet Corporation for Assigned Names and Numbers and the China Internet Network Information Center.

PRC law requires entities operating commercial websites to register their website names with the State Administration of Industry and Commerce or its local offices and obtain commercial website name registration certificates. If any entity operates a commercial website without obtaining such a certificate, it may be charged a fine or imposed other penalties by SAIC or its local offices. We have registered 14 website names used in connection with our online education business with Beijing Municipal Bureau of Industry and Commerce.

### ***Regulation of Bulletin Board Services***

Under the Administrative Measures on Internet Information Services and the Administrative Measures on Internet Bulletin Board Services adopted by MII on October 8, 2000, an Internet information services provider must obtain prior approval if it wishes to provide Internet bulletin board services. On July 4, 2010, the State Council promulgated the Decision on Canceling or Delegating the Fifth Batch of Administrative Examination and Approval Items, pursuant to which the administrative approval for providing Internet bulletin board service was cancelled.

### ***Regulation of Internet Publishing***

In June 2002, the State Press and Publications Administration and MII issued the Interim Provisions on Internet Publishing, or the Internet Publishing Regulations. The Internet Publishing Regulations require that all entities engaging in Internet publishing obtain approval from the State Press and Publications Administration before they can conduct any Internet publishing business. "Internet publishing" is broadly defined in the Internet Publishing Regulations as an act of online dissemination of works created by ICP license holders or others that such ICP license holders select, edit and process and subsequently post on the Internet or transmit to users via the Internet for browsing, reading, use or downloading by the public. These works include contents from books, newspapers, periodicals, audio-video products, electronic publications that have already been formally published or works that have been made public in other media or from the browsed and processed works relating to literature, art, nature science, social science, engineering technology and other aspects. The Internet Publishing Regulations include a requirement for Internet publishing organizations to have professional editorial personnel examine the contents being published to ensure that they comply with applicable laws. We believe we currently operate our business in a manner that complies with this regulation.

### ***Regulation of Privacy Protection***

PRC law does not prohibit Internet content providers from collecting and analyzing personal information from their users. PRC law prohibits Internet content providers from disclosing to any third parties any information transmitted by users through their networks unless otherwise permitted by law. If an Internet content provider violates these regulations, it may be liable for damages caused to its users and penalties or sanctions may be imposed by PRC governmental authorities including MII or its local counterparts. We believe we are in compliance with these regulations.

### ***Regulations on Protection of the Right of Dissemination through Information Networks***

On May 18, 2006, the State Council promulgated the Regulations on Protection of the Right of Dissemination through Information Networks, or the Dissemination Protection Regulations, which became effective on July 1, 2006. The Dissemination Protection Regulations require that every organization or individual who disseminates a third-party's work, performance, audio or visual recording products to the public through information networks shall obtain permission from, and pay compensation to, the copyright owner of such products, unless otherwise provided under relevant laws and regulations. The copyright owner may take technical measures to protect his or her right of dissemination through information networks and any organization or individual shall not intentionally evade, circumvent or otherwise assist others in evading such protective measures unless permissible under law. The Dissemination Protection Regulations also provide that permission from the copyright owners and compensation for the copyright-protected works is not required in the event of limited dissemination to teaching or research staff for the purpose of school teaching or scientific research only.

### ***Regulation of Online Cultural Activities***

The Ministry of Culture promulgated the Interim Provisions on Internet Culture, or the Internet Culture Provisions, in May 2003, which became effective on July 1, 2003 and was amended on July 1, 2004 and on February 11, 2011. The Internet Culture Provisions apply to all ICPs that engage in the production and dissemination of cultural products via the Internet. "Internet cultural activities" is defined in the Internet Culture Provisions as an act of provision of Internet cultural products and related services, which includes (i) the production, duplication, importation, and broadcasting of the Internet cultural products; (ii) the online dissemination whereby cultural products are posted on the Internet or transmitted via the Internet to end-users, such as computers, fixed-line telephones, mobile phones, television sets and games machines, for online users' browsing, use or downloading; and (iii) the exhibition and comparison of the Internet cultural products. In addition, "Internet cultural products" is defined in the Internet Culture Provisions as cultural products produced, broadcasted and disseminated via the Internet, which mainly include internet cultural products specially produced for the Internet, such as online music entertainment, online games, online shows and plays (programs), online performances, online works of art and online cartoons; and internet cultural products produced from cultural products such as music entertainment, games, shows and plays (programs), performances, works of art, and cartoons through certain techniques and duplicate those to internet for dissemination. All entities engaging in commercial Internet cultural activities, or Internet Cultural Entities, must be approved by the governmental agency of culture at the provincial level and by MII. Beijing Champion holds a Permit of Internet Cultural Activities issued by Beijing Municipal Bureau of Culture that is valid until December 31, 2014.

### ***Regulation of Online and Distance Education***

Pursuant to the Administrative Regulations on Educational Websites and Online and Distance Education Schools issued by MOE in 2000, or the Online Education Regulation, educational websites and online education schools may provide education services in relation to higher education, elementary education, pre-school education, teacher education, occupational education, adult education and other educational services. Under the Online Education Regulations, “Educational websites” refers to education websites providing education or education-related information services to website visitors by means of a database or an online education platform connected via the Internet or an educational television station through an Internet service provider, or ISP. Under the Online Education Regulations, “Online education schools” refer to organizations providing academic education services or training services with the issuance of various certificates.

Under the Online Education Regulations, setting up educational websites and online education schools is subject to approval from relevant education authorities, depending on the specific types of education provided. Under the Online Education Regulations, any educational website and online education school shall, upon receipt of approval, indicate on its website such approval information as well as the approval date and file number.

According to the Administrative License Law promulgated by the National People’s Congress on August 27, 2003 and effective as of July 1, 2004, only laws promulgated by the National People’s Congress and regulations and decisions promulgated by the State Council may establish administrative license requirements. On June 29, 2004, the State Council promulgated the Decision on Cutting Down Administrative Licenses for the Administrative Examination and Approval Items Really Necessary to be Retained, in which the administrative license for “online education schools” was retained, while the administrative license for “educational websites” was not retained.

Based on the opinion of our PRC legal counsel, Jingtian & Gongcheng, we believe that:

- None of Beijing Champion, Caikaowang and Champion Wangge is required to obtain a license to operate “educational websites” from the MOE under the current PRC laws or regulations;
- None of Beijing Champion, Caikaowang and Champion Wangge is required to obtain a license to operate “online education schools” because it does not offer through its website education services or training programs that directly offer government accredited academic degrees or other government accreditation certifications.

However, as the Administrative Regulations on Educational Websites and Online and Distance Education Schools has not been officially abolished, MOE or its local counterparts may continue to require online education providers like us to obtain approvals to run online education websites. If so required, we cannot assure you that such approvals can be obtained by us timely or at all.

### ***Regulation on the Wholesale, Retail and Rental of Book and Audio-Video Products***

Under the Administrative Measures for the Publication Market, or Administrative Measures, which was promulgated by the State Press and Publication Administration and became effective on September 1, 2003 and amended on June 16, 2004 and on March 17, 2011, any enterprise or individual wishing to engage in publication distributing activities must obtain permission from the press and publication agency at relevant levels. “Publication” and “distributing” are defined, respectively, in the Administrative Measures, as “books, newspapers, periodicals, audio-video products, and electronic publications” and “general distribution, wholesale, retail, rental, exhibition and other activities.” Any enterprise or individual who engages in publication wholesaler shall obtain a Publication Business License issued by the press and publication agency at the provincial level. A publication wholesaler enterprise can engage in retail distribution as well. Any enterprise or individual who engages in publication rental shall file a record at the county level of press and publication agency. Beijing Champion holds a Publication Business Permit for book wholesale issued by Beijing Press and Publication Bureau in February 2008 under which Beijing Champion is allowed to engage in the book wholesale and retail businesses. This permit was renewed in February 2011 and is valid through December 31, 2015.

### ***Regulations on Private Education***

The principal regulations governing private education in China consist of the Education Law of the PRC, the Law for Promoting Private Education (2003) and the Implementation Rules for the Law for Promoting Private Education (2004). These regulations are summarized below.

On March 18, 1995, the National People’s Congress promulgated the Education Law of the PRC, which became effective on September 1, 1995, or the Education Law. The Education Law stipulates that enterprises, social organizations and individuals are encouraged to operate schools and other types of educational organizations in accordance with the PRC laws and regulations. Meanwhile, no organization or individual may establish or operate a school or any other institution of education for profit-making purposes. However, private schools may be operated for “reasonable returns” as described in more detail below.

The Law for Promoting Private Education (2003) became effective on September 1, 2003, and the Implementation Rules for the Law for Promoting Private Education (2004) became effective on April 1, 2004. Under these regulations, “private schools” are defined as schools established by social organizations or individuals using non-government funds. In addition, private schools providing certifications, pre-school education, education for self-study aid and other academic education shall be subject to approval by the education authorities, while private schools engaging in occupational qualification training and occupational skill training shall be subject to approvals from the authorities in charge of labor and social welfare. A duly approved private school will be granted a Permit for Operating a Private School, and shall be registered with the Ministry of Civil Affairs of the PRC, or MCA or its local counterparts as a privately-run, non-enterprise institution. Champion Xinlixiang has obtained such a permit for independently operating a private school on May 11, 2011. This permit is valid through December 31, 2016.

Under the above regulations, private schools have the same status as public schools, though private schools are prohibited from providing military, police, political and other kinds of education which are of a special nature. In addition, the operation of private schools is highly regulated. For example, the types and amounts of fees charged by private schools offering certifications must be approved by the relevant governmental authority and be publicly disclosed, and the types and amounts of fees charged by private schools that do not offer certifications need only be filed with the relevant governmental authority and be publicly disclosed.

Private education is treated as a public welfare undertaking under the regulations. Nonetheless, investors in a private school may choose to require “reasonable returns” from the annual net balance of the school after deduction of costs, donations received, government subsidies, if any, the reserved development fund and other expenses as required by the regulations.

The election to establish a private school requiring reasonable returns shall be provided in the articles of association of the school. The percentage of the school’s annual net balance that can be distributed as reasonable returns shall be determined by the school’s board of directors, taking into consideration the following factors: (i) the school’s tuition and other fees, (ii) the ratio of the school’s expenses used for educational activities and improving the educational conditions to the total fees collected; and (iii) the school’s admission standards and educational quality. Information relating to the above factors shall be publicly disclosed before the school’s board determines the percentage of the school’s annual net balance that can be distributed as reasonable returns. This disclosed information and the decision to distribute reasonable returns shall also be filed with the approval authorities within 15 days from the decision made by the board. However, none of the current PRC laws and regulations provides a formula or guidelines for determining “reasonable returns.” In addition, none of the current PRC laws and regulations sets forth different requirements or restrictions on a private school’s ability to operate its education business based on such school’s status as a school that requires reasonable returns or a school that does not require reasonable returns. On July 29, 2010, the PRC central government, in the Outlines of China’s National Plan for Medium and Long Term Education Reform and Development promulgated by it, for the first time announced the policy that the government will implement a reform to divide private education entities into two categories: (i) for-profit private education entities and (ii) not-for-profit private education entities. However, this outline is still new and no further law or regulation has been promulgated to implement it yet.

At the end of each fiscal year, private schools are required to allocate a certain amount to their development fund for the construction and maintenance of the school and the procurement and upgrade of educational equipment. In the case of private schools that require reasonable returns, this amount shall be no less than 25% of the annual net income or the annual increase in the net assets of the school, while in the case of private schools that do not require reasonable returns, this amount shall be no less than 25% of the annual increase in the net assets of the school, if any. Private schools that do not require reasonable returns shall be entitled to the same preferential tax treatment as public schools. The regulations require that preferential tax treatment policies applicable to private schools requiring reasonable returns to be formulated by the finance authority, taxation authority and other authorities under the State Council, but to date no such regulations have been promulgated by the relevant authorities.

### ***Regulation of Foreign Exchange***

The PRC government imposes restrictions on the convertibility of the Renminbi and on the collection and use of foreign currency by PRC entities. Under current regulations, the Renminbi is convertible for current account transactions, which include dividend distributions, interest payments, and the import and export of goods and services. Conversion of Renminbi into foreign currency and foreign currency into Renminbi for capital account transactions, such as direct investment, portfolio investment and loans, however, is still generally subject to the prior approval of SAFE.

Under current PRC regulations, foreign-invested enterprises such as our PRC subsidiaries are required to apply to SAFE for a Foreign Exchange Registration Certificate for Foreign-Invested Enterprise. With such a certificate (which is subject to review and renewal by SAFE on an annual basis), a foreign-invested enterprise may open foreign exchange bank accounts at banks authorized to conduct foreign exchange business by SAFE and may buy, sell and remit foreign exchange through such banks, subject to documentation and approval requirements. Foreign-invested enterprises are required to open and maintain separate foreign exchange accounts for capital account transactions and current account transactions. In addition, there are restrictions on the amount of foreign currency that foreign-invested enterprises may retain in such accounts.



Further, SAFE promulgated a new circular (known as Circular 142) in August 2008 with respect to the administration of conversion of foreign exchange capital contributions of a foreign invested enterprise. The circular clarifies that Renminbi converted from foreign exchange capital contributions can only be used for the activities within the approved business scope of such foreign invested enterprise and cannot be used for domestic equity investments unless otherwise permitted.

### ***Regulation of Foreign Exchange in Certain Onshore and Offshore Transactions***

In October 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-Raising and Return Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies, or SAFE Circular 75, which became effective as of November 1, 2005. According to SAFE Circular 75, prior to establishing or assuming control of an offshore enterprise for the purpose of financing that offshore enterprise with assets or equity interests in an onshore enterprise in the PRC, each PRC resident, whether a natural or legal person, must complete certain overseas investment foreign exchange registration procedures with the relevant local SAFE branch. An amendment to the registration with the local SAFE branch is required to be filed by any PRC resident that directly or indirectly holds interests in that offshore enterprise upon either (i) the injection of equity interests or assets of an onshore enterprise to the offshore enterprise or (ii) any overseas fund-raising by such offshore enterprise after such injection. An amendment to the registration with the local SAFE branch is also required to be filed by such PRC resident when there is any material change involving a change in the capital of the offshore enterprise, such as (i) an increase or decrease in its capital, (ii) a transfer or swap of shares, (iii) a merger or division, (iv) a long-term equity or debt investment or (v) the creation of any security interests.

SAFE Circular 75 applies retroactively. As a result, PRC residents who established or acquired control of offshore companies that made onshore investments in the PRC in the past were required to complete the relevant overseas investment foreign exchange registration procedures by March 31, 2006. Under SAFE Circular 75, failure to comply with the registration procedures may result in restrictions on the relevant onshore entity, including restrictions on the payment of dividends and other distributions to its offshore parent or affiliate and restrictions on the capital inflow from the offshore entity, and may also subject relevant PRC residents to penalties under the PRC foreign exchange administration regulations.

As a Cayman Islands company, we are considered a foreign entity in China. If we purchase the assets or equity interests of a PRC company owned by PRC residents in exchange for our equity interests, such PRC residents will be subject to the registration procedures described in SAFE Circular 75. Moreover, PRC residents who are beneficial holders of our shares are required to register with SAFE in connection with their investment in us.

### ***Regulation of Overseas Listings***

On August 8, 2006, six PRC regulatory agencies, including the CSRC, promulgated the Regulation on Mergers and Acquisitions of Domestic Companies by Foreign Investors, which became effective on September 8, 2006 and was amended on June 22, 2009, or the M&A Rule. This M&A Rule, among other things, has certain provisions that require offshore special purpose vehicles, or SPVs, formed for the purpose of acquiring PRC domestic companies and controlled by PRC individuals, to obtain the approval of the CSRC prior to listing their securities on an overseas stock exchange. On September 21, 2006, the CSRC published on its official website a notice specifying the documents and materials that are required to be submitted for obtaining CSRC approval.

We believe, based on the opinion of our PRC legal counsel, Jingtian & Gongcheng, that while the CSRC generally has jurisdiction over overseas listings of SPVs like us, CSRC's approval was not required for our initial public offering given the fact that our current corporate structure was established before the M&A Rule became effective. There remains some uncertainty as to how the M&A Rule will be interpreted or implemented in the context of an overseas offering. If the CSRC or another PRC regulatory agency subsequently determines that approval was required for our initial public offering, we may face sanctions by the CSRC or another PRC regulatory agency. If this happens, these regulatory agencies may impose fines and penalties on our operations in the PRC, limit our operating privileges in the PRC, restrict or prohibit payment or remittance of dividends by our PRC subsidiaries to us or take other actions that could have a material adverse effect on our business, financial condition, results of operations, reputation and prospects, as well as the trading price of our ordinary shares. See "Item 3.D. Key Information — Risk Factors — General Risks Relating to Conducting Business in China — If the China Securities Regulatory Commission, or CSRC, or another PRC regulatory agency determines that its approval was required in connection with our initial public offering, we may become subject to penalties."

### ***Regulation of Security Review***

On February 3, 2011, the General Office of the State Council issued the Circular of the General Office of the State Council on the Establishment of Security Review System for Foreign Investors' Merger and Acquisition of Domestic Enterprises (the "Circular on the Establishment of Security Review"), which became effective on March 4, 2011. Among other things, the Circular on the Establishment of Security Review stipulates that the scope of the security review lies in foreign investors' acquisition of domestic military enterprises, military-related enterprises, enterprises involving sensitive military facilities and other enterprises that impact national defense security; foreign investors' acquisition of domestic enterprises which may provide foreign investors with de facto control over industries relating to national security, such as important agricultural products, energy and natural resources, infrastructures, transportation services, technologies and major equipment manufacturing. On August 25, 2011, the Ministry of Commerce issued the Circular of the Ministry of Commerce on the Implementation of Security Review System for Foreign Investors' Merger and Acquisition of Domestic Enterprises (the "Circular on the Implementation of Security Review"), which became effective on September 1, 2011. Among other things, the Circular on the Implementation of Security Review further specifies that whether a foreign investors' acquisition of domestic enterprises falls within the scope of the security review depends on the said transaction's substantive content and practical influence. Foreign investors shall not circumvent the security review through any arrangements or schemes, including but not limited to trust, lease and/or contractual arrangements.

According to our PRC counsel, as our contractual arrangements were established in 2003, the new security review system shall not apply to our contractual arrangements. We cannot guarantee, however, that the Ministry of Commerce will not promulgate additional implementing rules or new rules that will bring our contractual arrangements under the scope of the security review system. Moreover, according to a press conference held by the Ministry of Commerce on September 20, 2011, there are no specific laws or regulations governing contractual arrangements like the ones that we employ, but the Ministry of Commerce together with other authorities would study how to regulate them in the future. Hence, we cannot assure you that our contractual arrangements will not be subject to new regulations that will be issued by relevant regulatory authorities and that such new regulations will not cause any material adverse effect on our existing structure. See "Item 3.D. Key Information — Risk Factors — Risks Relating to Our Corporate Structure and Restrictions on Our Industry — Our contractual arrangements may be subjected to severe censorship under PRC laws and regulations and, thus, be challenged by relevant regulatory authorities."

### ***SAFE Regulations on Employee Share Options***

On March 28, 2007, SAFE promulgated the Application Procedure of Foreign Exchange Administration for Domestic Individuals Participating in Employee Share Holding Plan or Share Option Plan of Overseas Listed Company, or the Share Option Rule. The purpose of the Share Option Rule is to regulate foreign exchange administration of PRC domestic individuals who participate in employee share holding plans and share option plans of overseas listed companies. According to the Share Option Rule, if a PRC domestic individual participates in any employee share holding plan or share option plan of an overseas listed company, a PRC domestic agent or the PRC subsidiary of such overseas listed company shall, among others things, file, on behalf of such individual, an application with SAFE to obtain approval for an annual quota with respect to the purchase of foreign exchange in connection with share holding or share option exercises as PRC domestic individuals may not directly use overseas funds to purchase shares or exercise share options. Concurrent with the filing of such application with SAFE, the PRC domestic agent or the PRC subsidiary shall obtain approval from SAFE to open a special foreign exchange account at a PRC domestic bank to hold the funds required in connection with the share purchase or option exercise, any returned principal or profits from sales of shares, any dividends issued on the shares and any other income or expenditures approved by SAFE. The PRC domestic agent is also required to obtain approval from SAFE to open an overseas special foreign exchange account at an overseas bank to hold overseas funds used in connection with any share purchase or option exercise.

All proceeds obtained by PRC domestic individuals from sales of shares shall be remitted back to China after relevant overseas expenses are deducted. The foreign exchange proceeds from these sales can be converted into Renminbi or transferred to such individuals' foreign exchange savings account after the proceeds have been remitted back to the special foreign exchange account opened at the PRC domestic bank. If the share option is exercised in a cashless exercise, the PRC domestic individuals are required to remit the proceeds to the special foreign exchange account.

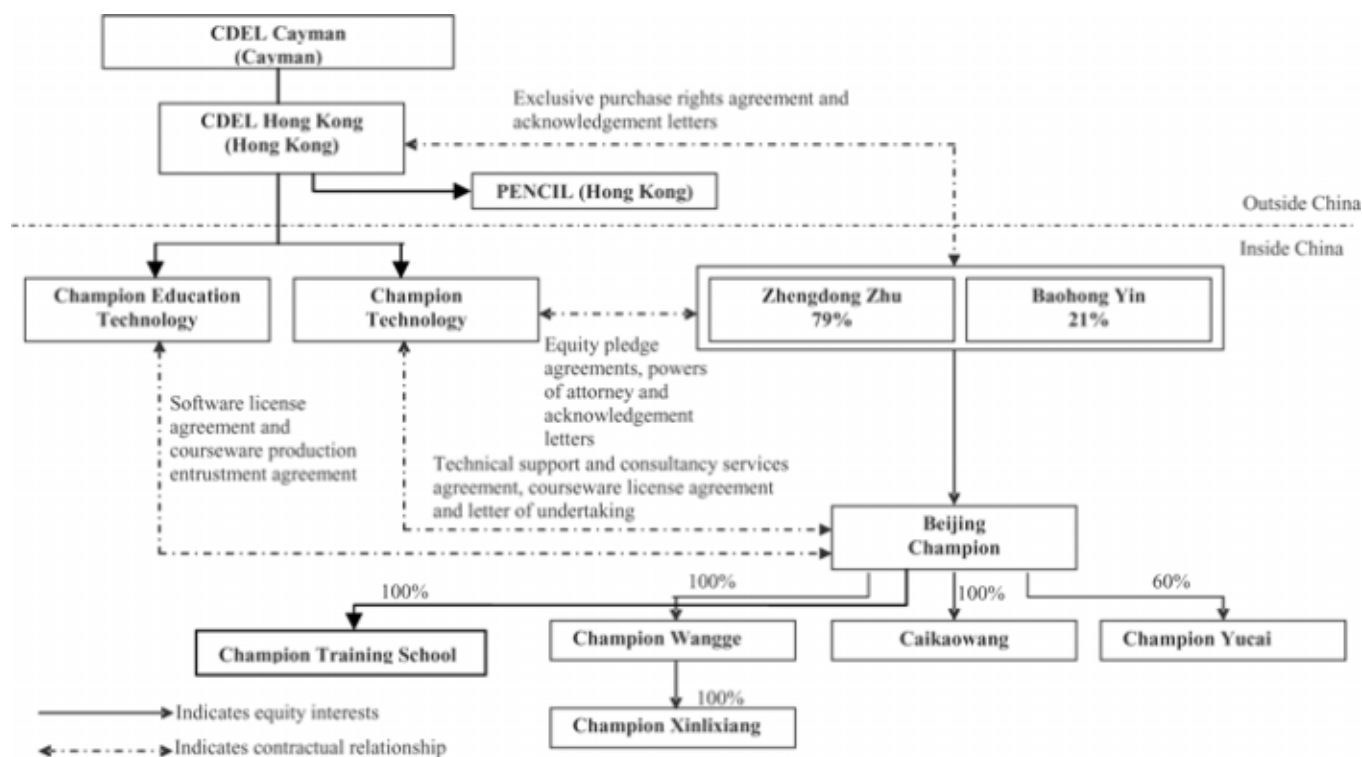
Although further clarification is required as to how the Stock Option Rule will be interpreted or implemented, we believe that we and our PRC employees who have been granted share options are subject to the Share Option Rule. If we or our PRC employees fail to comply with the Share Option Rule, we and/or our PRC employees may face sanctions imposed by foreign exchange authority or any other PRC government authorities.

In addition, the State Administration of Taxation has issued a few circulars concerning employee share options. Under these circulars, our employees working in China who exercise share options will be subject to PRC individual income tax. Our PRC subsidiaries have obligations to file documents relating to employee share options with relevant tax authorities and withhold individual income taxes of those employees who exercise their share options. If our employees fail to pay and we fail to withhold their income taxes, we may face sanctions imposed by tax authorities or other PRC government authorities.

### C. Organizational Structure

Due to PRC legal restrictions on foreign ownership and investment in the Internet content distribution industry in China, we operate our online education business through Beijing Champion, a domestic Chinese company owned by Zhengdong Zhu and Baohong Yin, both of whom are PRC citizens. CDEL Hong Kong, Champion Technology and Champion Education Technology, all of which are our wholly owned subsidiaries, have entered into a series of contractual arrangements with Beijing Champion and its shareholders, including a technical support and consultancy services agreement, an exclusive purchase rights agreement, a courseware license agreement, a software license agreement, a courseware production entrustment agreement, a letter of undertaking from Beijing Champion's two shareholders to Champion Technology, a letter from Champion Technology to Beijing Champion, declaration letters, power of attorneys, acknowledgement letters to us and acknowledgement letters to Champion Technology from each of Beijing Champion's shareholders, and a notice to Beijing Champion and its shareholders from Champion Technology. These contractual arrangements also include equity pledge agreements (as amended and restated) entered into with each of the shareholders of Beijing Champion. As a result of these contractual arrangements, we have the power to direct the activities of, and have the right to receive benefits from, Beijing Champion, and accordingly, under U.S. GAAP, we consolidate Beijing Champion's operating results in our consolidated financial statements.

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



The following is a summary of the material provisions of these agreements. For more complete information you should read these agreements in their entirety. Directions on how to obtain copies of these agreements are provided in this annual report under "Item 10.H. Additional Information — Documents on Display."

#### **Agreements that transfer economic benefits of the controlled affiliates and their subsidiaries to the Company**

*Technical Support and Consultancy Services Agreement*, dated May 1, 2004. Under this agreement, Champion Technology provides Beijing Champion with exclusive technical support and consultancy services relating to Beijing Champion's online education business. The services rendered by Champion Technology mainly include assisting in course creation and production, undertaking pre-paid study card production, advising on website design and maintenance, providing general technology support and technical personnel training, assisting in strategic planning and business development and establishing and implementing a customer service system. In return, Beijing Champion pays Champion Technology a monthly service fee, which is equal to Beijing Champion's revenues less its cost of sales and operating and other expenses as approved by Champion Technology. In addition, Beijing Champion undertook not to approve its annual budget, or engage in any transactions that could materially affect Beijing Champion's capital structure, assets, liabilities, rights or operations, without the prior written consent of Champion Technology. Champion Technology undertook to provide financial support at Beijing Champion's request in a manner permitted by law. This agreement will remain effective until Beijing Champion ceases its operations.

*Letter of Undertaking from Beijing Champion's Shareholders to Champion Technology*, dated February 13, 2008. Pursuant to this letter addressed to Champion Technology, the shareholders of Beijing Champion undertook to, unless restricted by laws, regulations or legal procedures, (i) remit all dividends, interests, other distributions or remnant assets after liquidation, if any, they receive from Beijing Champion to Champion Technology without compensation, after paying the corresponding tax and any other required expenses, (ii) transfer all or part of their equity interests to CDEL Hong Kong at a nominal or minimal purchase price, in the event CDEL Hong Kong exercises its exclusive purchase right to acquire any or all of the equity interests in Beijing Champion, (iii) remit to Champion Technology all considerations they may receive from CDEL Hong Kong's acquisition of any equity interests in Beijing Champion, without compensation, after paying the corresponding tax and any other required expenses and (iv) act in the best interest of Champion Technology.

*Declaration Letters*, dated March 24, 2008. Pursuant to these letters, the shareholders of Beijing Champion acknowledged that the distribution of dividends in March 2005 in the amount of \$0.7 million was a one-time distribution of all dividends accrued prior to the execution of the technical support and consultancy services agreement described above. The shareholders of Beijing Champion undertook that after the aforesaid one-time dividend distribution, they will, unless restricted by law, remit all dividends they may receive from Beijing Champion to Champion Technology after paying applicable tax and other required expenses.

*Software License Agreement*, dated May 20, 2007. Pursuant to this agreement, Champion Education Technology granted Beijing Champion a non-exclusive license to use the online course delivery platform for the duration of its operating period. In return, Beijing Champion pays Champion Education Technology a license fee calculated based on the revenues generated from the use of the platform.

*Courseware Production Entrustment Agreement*, dated May 20, 2007. Pursuant to this agreement, Champion Education Technology provides Beijing Champion with services of editing, production, compilation, updating and maintenance of courseware. As consideration, Beijing Champion pays Champion Education Technology a fee calculated based on an hourly rate.

#### ***Agreements that provide the Company effective control over the controlled affiliates and their subsidiaries***

*Equity Pledge Agreements*, entered into on May 1, 2004 and amended and restated on December 31, 2008. To secure the payment obligations of Beijing Champion under the technical support and consultancy services agreement described above, each of Beijing Champion's shareholders, Mr. Zhu and Ms. Yin, pledged to Champion Technology his or her entire equity ownership interests in Beijing Champion pursuant to an Equity Pledge Agreement entered into on May 1, 2004, or the May 2004 Equity Pledge Agreement. In May 2008, Mr. Zhu and Ms. Yin contributed an additional RMB16.8 million (\$2.5 million) to Beijing Champion as increased registered capital. In connection with such capital contribution to Beijing Champion, each of Mr. Zhu and Ms. Yin amended and restated his or her May 2004 Equity Pledge Agreement on December 31, 2008, or the Amended and Restated Equity Pledge Agreement. Each of the Amended and Restated Equity Pledge Agreements could only become effective, and replace the respective May 2004 Equity Pledge Agreement, after the pledge created thereunder is registered with SAIC or its local office. We successfully registered the pledge created under each of the Amended and Restated Equity Pledge Agreements with the Beijing office of SAIC on January 12, 2009. Upon the occurrence of certain events of default specified in the Amended and Restated Equity Pledge Agreements, the pledgee may exercise its rights and foreclose on the pledged equity interest. Under such agreements, the pledgor may not transfer the pledged equity interests without the pledgee's prior written consent. The agreements will also be binding upon successors of the pledgors and transferees of the pledged equity interests. These agreements will remain effective until the discharge of Beijing Champion's contractual obligations under the technical support and consultancy services agreement as described above.

*Exclusive Purchase Rights Agreement*, dated May 9, 2004. Pursuant to the exclusive purchase rights agreement entered into among CDEL Hong Kong, Beijing Champion and its shareholders, CDEL Hong Kong or any third-party designated by it has the right to acquire, in whole or in part, the respective equity interests in Beijing Champion of its shareholders when permitted by applicable PRC laws and regulations. The term of this agreement is ten years from the date thereof and can be extended for another ten years at the discretion of CDEL Hong Kong.

*Powers of Attorney*, dated March 25, 2008. Pursuant to these powers of attorney, each shareholder of Beijing Champion authorized Champion Technology or any person it designates to (i) exercise all voting powers that such shareholder enjoys under the laws and the articles of association of Beijing Champion, including the sale, transfer or pledge, in whole or in part, of such shareholder's equity interests in Beijing Champion; (ii) nominate and appoint, on behalf of such shareholder, the legal representative, directors, supervisors, general manager, and other senior management of Beijing Champion; (iii) execute the share transfer agreement as contemplated by the exclusive purchase rights agreement described above, and perform the equity pledge agreement and the exclusive purchase rights agreement described above; and (iv) authorize any third party to carry out any of the above actions. In addition, the shareholders undertook to refrain from exercising any of the above-mentioned rights.

*Notice to Beijing Champion and its Shareholders*, dated March 25, 2008. Pursuant to this notice, Champion Technology authorized Zhengdong Zhu to exercise all rights and powers granted by the powers of attorney described above.

*Acknowledgement Letter to Champion Technology*, dated March 25, 2008. Pursuant to this acknowledgement letter, the shareholders of Beijing Champion acknowledged that their contribution of RMB3.2 million (\$0.5 million) to the registered capital of Beijing Champion prior to May 1, 2004 is subject to the equity pledge agreements described above.

*Acknowledgement Letter to CDEL Cayman*, dated March 25, 2008. Pursuant to this acknowledgement letter, the shareholders of Beijing Champion acknowledged their contribution of \$0.5 million (equivalent to RMB3.2 million) to CDEL Hong Kong in May 2004 is subject to the equity pledge agreements described above.

#### ***Other agreements among the Company's subsidiaries and the controlled affiliates***

*Courseware License Agreement*, dated August 1, 2004. Pursuant to this agreement, Beijing Champion granted Champion Technology an exclusive license to use specific distance education and training courseware owned by Beijing Champion free of charge. Under this agreement, Champion Technology is granted the rights to use the courseware for the duration of its operating period.

*Letter of Undertaking from Champion Technology to Beijing Champion*, dated February 13, 2008. Pursuant to this letter, Champion Technology confirmed its obligation to provide financial support to Beijing Champion if Beijing Champion suffers any financial loss.

For risks associated with our contractual arrangements with Beijing Champion and its shareholders, see “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Corporate Structure and Restrictions on Our Industry.”

#### **D. Property, Plants and Equipment**

Our principal executive offices are located in approximately 2,495 square meters of office space on the 18<sup>th</sup> floor, Xueyuan International Tower, No. 1 Zhichun Road, Haidian District, Beijing, 100083, China. We also own approximately 355 square meters of office space in Hangzhou, China. We also lease approximately 4,090 square meters at the Xueyuan International Tower and 37,511 square meters at different locations of China. We believe that our existing facilities are adequate for our current requirements and that additional space can be obtained on commercially reasonable terms to meet our future requirements.

#### **ITEM 4A. UNRESOLVED STAFF COMMENTS**

Not applicable.

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

The following discussion of our financial condition and results of operations is based upon and should be read in conjunction with our consolidated financial statements and their related notes included in this annual report on Form 20-F. This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. See “Introduction — Forward Looking Statements.” In evaluating our business, you should carefully consider the information provided under “Item 3.D. Key Information — Risk Factors.” We caution you that our business and financial performance are subject to substantial risks and uncertainties.

The selected consolidated statements of operations data for the fiscal years ended September 30, 2009, 2010 and 2011 (other than ADS data) and the selected consolidated balance sheets data as of September 30, 2010 and 2011 reflect the Retrospective Adjustments. Where applicable, the selected consolidated statements of operations data for the fiscal years ended September 30, 2009 and 2010 that have been retrospectively adjusted are followed by “(adjusted)” where they differ from those reported in our prior year’s annual report on Form 20-F. See “—Operating Results—Loss from discontinued operations” for more information. Due to the Retrospective Adjustments, our results of operations for the years ended September 30, 2007, 2008, 2009, and 2010 and financial positions as of September 30, 2007, 2008, 2009, and 2010 are not directly comparable to the prior reporting periods.

#### **A. Operating Results**

##### **Overview**

We offer a wide range of online education and test preparation courses and other related services and products. Our online courses are designed to help professionals and other course participants obtain and maintain the skills, licenses and certifications necessary to pursue careers in China in the areas of accounting, law, healthcare, construction engineering and other industries. We also offer test preparation courses to self-taught learners pursuing higher education diplomas or degrees and to secondary school and college students preparing for various academic and entrance exams. We further offer online foreign language courses. Our online education courses, accounted for 74.0%, 73.6% (adjusted) and 74.1% of our net revenues in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. In addition, we also further expanded our course offerings into offline areas, including offline primary and secondary school supplementary courses and business start-up training courses. In addition, we sell books and reference materials through third-party bookstores and distributors across China and, to a lesser extent, through our online bookstore and our offices in Beijing. We also, from time to time, provide course production services, platform production services and magazine content production services for certain customers at their request, and provide in-person accounting and healthcare professional training to accounting firms and the general public.

To comply with PRC law, we have adopted a corporate structure whereby we operate our business through a series of contractual arrangements with Beijing Champion, a PRC entity owned by Zhengdong Zhu, our co-founder, chairman and chief executive officer, and his wife, Baohong Yin, our co-founder and deputy chairman. As a result, we do not enjoy direct equity ownership of Beijing Champion, our primary consolidated operating company. However, through these contractual arrangements, we effectively control Beijing Champion and its subsidiaries and consolidate its financial results in our consolidated financial statements, and thus references to “we,” “us,” “our company” and “our” refer not only to China Distance Education Holdings Limited and its subsidiaries, but also to Beijing Champion and its subsidiaries as the context requires. For a more detailed discussion of these contractual arrangements, see “Item 4.C. Information on the Company — Organizational Structure,” and for a detailed description of the regulatory environment for Internet-based businesses in China that necessitates our adoption of this structure, see “Item 4.B. Information on the Company — Business Overview — Regulations.” In addition, for a detailed description of the risks associated with our corporate structure and these contractual arrangements that support our corporate structure, see “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Corporate Structure and Restrictions on Our Industry.”

Our net revenues were \$30.1 million, \$32.6 million (adjusted), and \$41.6 million in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. Our net income was \$1.2 million in the fiscal year ended September 30, 2009. We incurred net losses of \$1.9 million and \$3.8 million in the fiscal years ended September 30, 2010 and 2011, respectively. Our net loss during the fiscal year ended September 30, 2010 compared to the net income in the fiscal year ended September 30, 2009 resulted mainly from additional share-based compensation expenses arising from our share options granted in the first quarter of the fiscal year ended September 30, 2010, impairment of goodwill, intangible assets and purchased call options acquired with the acquisitions of Zhengbao Yucai and Champion Xinlixiang and a \$2.2 million bad debt provision made for certain accounts receivables that have been outstanding for more than 360 days with respect to the business start-up training business, accounting continuing education courses and information technology application training, or ITAT, contest. Our higher net loss during the fiscal year ended September 30, 2011 compared to the fiscal year ended September 30, 2010 stemmed mainly from share-based compensation expenses arising from the re-pricing and acceleration of the vesting of our share options granted under the Prior Plan in the fourth quarter of the fiscal year ended September 30, 2011, and impairment of goodwill, property, plant and equipment, intangible assets and purchased call options acquired with the acquisitions of Zhengbao Yucai and Champion Xinlixiang. Our total course enrollments increased from approximately 1,134,000 for the fiscal year ended September 30, 2009 to over 1,215,000 and 1,601,000 for the fiscal years ended September 30, 2010 and 2011, respectively.

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

We have benefited significantly from overall economic growth and the expansion of the education market. Economic growth and increasing consumer consumption in China have contributed to a significant increase in spending on education. Furthermore, China’s integration into the global economy and growth in China’s professional services sector are driving demand for qualified talent in China, particularly in the areas of accounting, law, healthcare, construction engineering and financial services. We have also benefited from increasing Internet and broadband penetration rates in China, which have increased the acceptance of online education and training courses as an effective and convenient way for people to meet their educational and career development needs. However, any adverse changes in the economic conditions or regulatory environment in China may have a material adverse effect on the Internet services industry and the education industry in China, which in turn may adversely affect our results of operations.

Our results of operations may also be affected by other factors such as changes to the license, qualification, knowledge and skill requirements applicable to the various disciplines and professions covered by our online courses, and changes in the timing, content and difficulty, or perceived difficulty, of exams covered by our courses, changes in the continuing education requirements, and changes in the government subsidy policy applicable to our business start-up training courses. Exams covered by our courses may also, from time to time, be discontinued or postponed for reasons beyond our control, which may impact our revenues in certain periods. See “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — Our business could be adversely affected by changes in the perceived difficulty, requirements or formats of professional examinations and continuing education in China,” “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — Our business could be adversely affected by changes in the perceived difficulty, requirements or formats of business start-up training courses, or changes in the government authorities’ subsidy policy” and “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — Our financial performance and prospects could be affected by natural calamities or health epidemics.” We also typically experience lower revenues in the quarters ending December 31 and March 31 than in the quarters ending June 30 and September 30 due to the timing of exams covered by our courses. See “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — Our business is subject to seasonal fluctuations, which may cause our operating results to fluctuate from quarter to quarter. This may result in volatility in and adversely affect the price of our ADSs.” Our results of operations could also be impacted by fluctuations in exchange rates. See “Item 3.D. Key Information — Risk Factors — General Risks Relating to Conducting Business in China — Fluctuations in exchange rates could result in foreign currency exchange losses.” In addition, our results of operations could be impacted by share-based compensation expenses arising from share options and/or restricted shares granted under our share incentive plans. See “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Business — We may continue to grant share options and/or restricted shares under our current or future share incentive plans, or modify the terms of existing share options, which may continue to materially impact our future results of operations or result in dilution to our shareholders.”

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

Our results of operations in any given period are also directly affected by company-specific factors, including:

- *Number of enrollments in our courses.* Our ability to generate and grow our net revenues is primarily affected by our ability to increase the number of course enrollments. This in turn is driven by several factors, including governmental and industrial requirements for education and training in various professions and industries, recognition of our brand and services, Internet and broadband penetration rate, and the perceived effectiveness of our education and training courses. Government regulations requiring increased number of licensure and certification exams provide us with new market opportunities to develop new courses and to attract potential exam participants as our customers. Changes in exam content and knowledge requirements in certain industries and professions, and the increased difficulty, or perceived difficulty of certain exams covered by our courses, may also contribute to growth in our course enrollments as more exam takers may feel a stronger need to take exam preparation courses. Government policies encouraging business start-up training provide us with new market opportunities to develop new courses and to attract potential course participants to take our courses. Benefiting from the above driving factors, our total course enrollments increased from approximately 1,134,000 for the fiscal year ended September 30, 2009 to 1,215,000 and 1,601,000 for the fiscal years ended September 30, 2010 and 2011, respectively.

However, we may also, from time to time, experience a decrease in course enrollments in certain subject areas if there is a perception within those industries or professions that certain exams have become less difficult, or the content more routine and familiar, and as a result these exam takers may be less inclined to spend additional money on test preparation courses. For example, our Accounting Professional Qualification Examination online course enrollments decreased from approximately 209,000 for the fiscal year ended September 30, 2007 to approximately 197,000 for the fiscal year ended September 30, 2008 and further decreased to approximately 193,000 in the fiscal year ended September 30, 2011. This decrease occurred primarily because we experienced a significant increase in enrollments in these accounting courses during the fiscal year ended September 30, 2007 due to the fact that the relevant accounting exams covered by these courses at the time were undergoing changes in content and requirements, and many exam takers determined that enrolling in our online courses was important to their exam preparation efforts. In the subsequent period, as exam takers became more familiar with and less concerned about the new exam content and requirements, many exam takers opted not to take our courses, which resulted in a decrease in course enrollments of these courses. Another example was our CPA Qualification Examination of which online course enrollments decreased from approximately 120,000 in the fiscal year ended September 30, 2010 to approximately 111,000 in the fiscal year ended September 30, 2011.

In addition, although overall enrollment in our online elite classes increased from approximately 6,400 in the fiscal year ended September 30, 2010 to approximately 9,000 in the fiscal year ended September 30, 2011, enrollment in our online elite classes for our accounting, higher-education for self-taught learners and legal courses decreased in the fiscal year ended September 30, 2010 as an increasing number of course participants chose to register for our premium classes, which they consider more suitable for their needs. For example, course enrollment in our online CPA Qualification Examination and Intermediate Level Accounting Professional Qualification Examination elite classes decreased from approximately 1,600 and 1,500 in the fiscal year ended September 30, 2009 to approximately 700 and 1,300 in the fiscal year ended September 30, 2010. Meanwhile, course enrollments in most of our online premium classes experienced steady increases. However, we expect overall demand for our courses to continue to increase, especially for accounting continuing education and self-taught study process monitoring programs, due to an increasing number of individuals seeking to enter or obtain various qualifications applicable to the professions and industries covered by our courses and those seeking to fulfill regulatory or admission requirements. Finally, any government decisions to scale back, postpone or cancel certain exams, combine exams or adopt measures that might reduce the number of exam participants may adversely impact our revenues.

- *Fees for our courses.* Our net revenues are also affected by the amount of fees we charge for our courses, which depends on the overall demand, the prices and availability of competing courses, perception of the quality and effectiveness of our courses and the income levels that our course participants expect to achieve upon passing the related licensure and certification exams. We may also experience pricing pressure as we expand our course offerings into new areas, or new segments and exams within existing areas that we cover, to attract new customers. In addition, our net revenue generated from our business start-up training course is affected by our entitlement to government subsidy payments conditioned on our ability to meet government stipulated conditions under their subsidy policies. Such stipulated conditions include the pass rate of our course participants' business proposals as evaluated by the relevant government authorities, the business start-up rate and the employment rate of our business start-up course participants.

- *Our ability to expand the range of courses and other services.* Our ability to address market needs in new areas, or in new segments and exams within existing areas we cover by expanding the range of our course offerings and other services, has a direct impact on our ability to maintain rapid growth in our course enrollments. Diversifying our sources of revenues also helps protect us from possible down-turns in certain industries or professions. To date, our accounting courses remain the largest and most important of all our course offerings in terms of revenues and numbers of course enrollments. Although we expect the accounting profession to remain a stable source of customers for our services due to the large and increasing number of industry participants and the existence of various qualification exams and professional requirements in the industry, we have expanded and plan to continue to expand our course offerings to further grow our revenues, expand our brand and reputation into other areas, and provide a buffer against over-reliance on any one particular area. Over the past several years, we have developed our legal and healthcare course offerings and further enhanced the reputation of our other course offerings in the areas of construction engineering, primary and secondary school supplementary courses and business start-up training courses.
- *Impact of strategic alliances and business acquisitions.* We have pursued and may continue to pursue strategic alliance and acquisition opportunities to increase our service offerings and expand our growth. In March 2009, we acquired the business start-up training business from Beijing Yinglun Yucai Education Consulting Co., Ltd., or Yinglun Yucai, which was owned by Mr. Liang Ma, a third-party individual. The acquired business is operated by Zhengbao Yucai, an entity established by Beijing Champion. With an initial consideration of RMB36.0 million (\$5.3 million), we are entitled to 60% of the ownership interest of Zhengbao Yucai. In January 2010, we sought through arbitration to require Mr. Liang Ma, Yinglun Yucai, and Global Education Consortium Group Co., Limited, to compensate us for the loss incurred as a result of their failure to perform the related agreement. In June 2011, China International Economic and Trade Arbitration Commission ruled, among other things, that Mr. Liang Ma shall surrender his 40% ownership interest in Zhengbao Yucai to us for no consideration. For more information with respect to this acquisition, please see “Item 8. Financial Information-Legal Proceedings.” In September 2009, we acquired the business of Gaokao retake preparation and high-school supplementary tutoring business from Mr. Junnan Ye and Mr. Xiujie Hu, two third-party individuals. The acquired business is operated by Champion Xinlixiang, an entity established by Champion Wange. With an initial consideration of RMB16.0 million (\$2.4 million), we were entitled to 60% of the ownership interest of Champion Xinlixiang. In November 2010, we agreed with Mr. Junnan Ye and Mr. Xiujie Hu that the profit target for the fiscal year 2010 as stipulated in the original purchase agreement was not met by Champion Xinlixiang. Accordingly, pursuant to the terms of the original purchase agreement, Mr. Junnan Ye and Mr. Xiujie Hu surrendered their 40% ownership interest in Champion Xinlixiang to us for no consideration on October 1, 2010. Similar acquisitions may not generate the financial results we expect and may even result in losses. With respect to our Gaokao retake preparation and high-school supplementary tutoring business, we have suffered significant operating losses for the fiscal year ended September 30, 2011 and decided to discontinue such business and put the related assets and business up for sale.

We also often enter into strategic alliances with global education leaders as their exclusive distributor in China. Examples of these strategic alliances include our alliance with Becker Professional Education where we exclusively distribute Becker Professional Education’s CPA Review and CPA Final Review courses and related materials in China. More recently, we also entered two strategic alliances with AsknLearn Pte. Ltd., a subsidiary of Educomp Solutions (“Educomp”) and TStudy Co., Ltd. (“TStudy”) whereby we obtained the exclusive right to distribute their respective products. Under the agreement with Educomp, we obtained exclusive rights to distribute Educomp’s Smart Class®, Edulearn and Wizlearn products in China. Under the agreement with TStudy, we gained the exclusive distribution right for its proprietary digital educational products and software, including Symphony, TStudy Interactive Whiteboard, Dotnote and Tnote in China. Our ability to successfully identify, execute, integrate and manage new alliances and acquisitions can have a significant effect on our results of operations.



## Description of Key Line Items

### Net Revenues

We derive net revenues from the sale of online education services, books and reference materials, and other related products and services such as course production services, platform production services, magazine content production services, in-person accounting and healthcare professional training to accounting firms and public, offline primary and secondary school supplementary courses, business start-up training courses, and accounting and tax consulting services. Our net revenues are presented net of PRC business tax and related surcharges, as well as value-added taxes. The following table sets forth a breakdown of our total net revenues for the periods indicated:

	Year Ended September 30,					
	2009		2010 (adjusted)		2011	
	\$	% of net revenues	\$	% of net revenues	\$	% of net revenues
Net Revenues	(In thousands, except for percentages)					
Online education services	22,279	74.0%	23,982	73.6%	30,788	74.1%
Books and reference materials	2,709	9.0%	3,939	12.1%	4,743	11.4%
Others	5,133	17.0%	4,658	14.3%	6,033	14.5%
Total net revenues	30,121	100.0%	32,579	100.0%	41,564	100.0%

### Online Education Services

We derive most of our revenues from the provision of online education services. Our online education services consist of online professional education and test preparation courses, test preparation courses for self-taught learners pursuing higher education diplomas or degrees and secondary school and college students preparing for various academic and entrance exams, continuing education courses for professionals fulfilling regulatory requirements, and language courses. Our professional training courses cover a wide range of industries, including accounting, law, healthcare, construction engineering and others.

We earn revenues from course fees paid by course participants enrolled in our online education courses. We recognize course fee payments as revenues pursuant to one of two types of revenue recognition models, the non-refundable course model and the refundable course model. The non-refundable course model represents our original revenue recognition model used for our courses since the start of our business, including for the three fiscal years ended September 30, 2009, 2010 and 2011. This revenue recognition model applies to most of our current courses. For online courses with exams using the non-refundable course model, we recognize revenues on a straight line basis over the subscription period from the date on which the course participants enroll in the courses to the completion date of the relevant exam when we close access to the relevant online course materials except that we recognize part of our revenues of accounting continuing education when course participants complete the stipulated study hours and take the examinations. With respect to courses without exams using the non-refundable course model, we recognize revenues on a straight line basis over the subscription period during which the courses are delivered to the participants.

We adopted the refundable course model in the fiscal year ended September 30, 2007 to recognize revenues generated from our “elite” classes, which were first introduced in November 2006. With our elite classes, course participants pay substantially higher course fees for more personal and tailored course-related services. After completing an elite class, if a participant fails to pass the exam subject that the course prepares him or her for, and certain pre-agreed conditions are met, the course participant is then entitled to a refund of the applicable course fee paid, which amount the course participant can choose to claim in the form of a cash refund or apply to future courses provided by us. For courses using the refundable course model, the proceeds from the refundable course model are initially recorded as refundable fees, and thereafter we recognize revenues upon the expiration of the course participants’ right to receive a refund or the right to retake the course.

We introduced our premium classes under the non-refundable course model in August 2008 for some of our most successful courses, such as courses for the accounting, legal and healthcare industries. Our premium class participants enjoy high-quality premium course-related support services similar to the elite class participants. However, premium course participants do not enjoy refund privileges. Instead, in general, if a participant fails to pass the course examination and certain pre-agreed conditions are met, the course participant can retake the same premium course and pay only 50% of the course fees. The participant is given this 50% discount only once, therefore, if he or she fails the relevant course examination again and wishes to retake the premium course for the third time, there is no discount provided at that time. If a participant fails to pass the course examination for the examinations of American Institute of CPAs and certain healthcare courses, however, the course participant can retake the same courses free of charge for the following year if certain pre-agreed conditions are met.

To enroll in our courses, course participants may choose to purchase pre-paid study cards from our distributors or to pay us through bank remittance, postage, online payment using credit or debit cards via external payment networks or cash at our offices. We provide course participants with a one-week trial period, applicable to the foundation classes of most courses that we offer, commencing on the date course participants activate their subscription for the relevant course. If course participants decide within the one-week trial period that they no longer want to take the course, we will refund their course fees. The amount of one-week trial period course fee refunds was insignificant in the fiscal years ended September 30, 2009, 2010 and 2011. We begin to recognize revenues following the expiry of the one-week trial period.

To use the face value on a pre-paid study card, course participants must activate the card by using an access code and password to transfer the face value on the card to their personal online registered accounts and register for the desired courses. We first introduced pre-paid study cards in January 2003. Our study cards are sold with expiration dates, typically set at two to three years from the print date of the card. Proceeds from the expired study cards that have never been activated are recognized as revenues upon expiration of the cards. For the fiscal years ended September 30, 2009, 2010 and 2011, we recognized revenue before business tax and related surcharges in connection with expired pre-paid study cards of approximately \$90,000, \$90,000 and \$103,000, respectively. Once course participants activate the pre-paid study cards, the face values of the cards are added to their personal registered accounts and are no longer subject to expiration. We, at times, offer volume discounts to our distributors for purchases over a specified amount of pre-paid cards during a specified period of time, generally one year. These discounts are provided to distributors in the form of additional study cards. The after-discount prices of the study cards paid by the distributors to us are recognized as deferred revenue. Deferred revenue is subsequently recognized as revenues upon provision of the future services according to the applicable revenue recognition policy discussed above.

### ***Books and Reference Materials***

We primarily sell our own proprietary learning materials relating to accounting professional courses and exams through third-party bookstores and distributors and, to a lesser extent, directly through our online bookstore and at our offices in Beijing. We began selling books and reference materials in 2003. The sale of books and reference materials on topics related to our course subject matter complements our online course offerings, supplements the learning experience of our course participants, and helps build brand recognition and loyalty among our customers. The books and reference materials we sell are not compulsory for students taking the online course or the examination. In addition, our proprietary books help promote our expertise and reputation in the accounting field.

Our sales arrangements are evidenced by sales agreements with and purchase orders from distributors. We recognize revenues from the sale of books and reference materials when the four criteria as discussed under “Critical Accounting Policies — Revenue Recognition” below are met.

Starting from the fiscal year ended September 30, 2009, we sold some of our books and reference materials together with study cards that can be used to enroll in particular online courses.

### ***Others***

We derive other net revenues from the provision of offline education services, course production services, platform production services, and others including magazine content production services, advertising services, and consulting services. Such sales arrangements, except for the business start-up training courses, are evidenced by individual sales agreements with customers. We do not charge course participants fees for attending our business start-up training courses. Instead, we receive subsidies from the relevant government authority, which are conditioned on our ability to meet government stipulated conditions under the subsidy policies. For more information, see “Item 4 Information on the Company — Business Overview — Business Start-up Training Courses”.

### **Cost of Sales**

Our cost of sales consists of cost of services and cost of tangible goods sold. The following table shows our cost of sales, gross profit and gross margin for the periods indicated.

	For the Year Ended September 30,					
	2009		2010 (adjusted)		2011	
	\$	% of net revenues	\$	% of net revenues	\$	% of net revenues
(In thousands of \$, except for percentages)						
Net Revenues	30,121	100.0%	32,579	100.0%	41,564	100.0%
Cost of sales:						
Cost of services	(12,834)	(42.6)%	(13,283)	(40.8)%	(16,840)	(40.5)%
Cost of tangible goods sold	(1,577)	(5.2)%	(2,070)	(6.3)%	(2,794)	(6.7)%
Total cost of sales	(14,411)	(47.8)%	(15,353)	(47.1)%	(19,634)	(47.2)%
Gross profit and gross margin <sup>1</sup>	15,710	52.2%	17,226	52.9%	21,930	52.8%

<sup>1</sup> Gross profit is equal to net revenues less cost of sales. Gross margin is equal to gross profit divided by net revenues.

### ***Cost of Services***

Cost of services accounted for 42.6%, 40.8% (adjusted) and 40.5% of our net revenues in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. Cost of services are mainly composed of salaries and related expenses for our tutors, course production technicians and other employees, fees paid to our course lecturers, rental and related expenses, server management and bandwidth leasing fees paid to third-party providers, and depreciation and amortization expenses. Our cost of services as a percentage of net revenues decreased in the fiscal year ended September 30, 2010 compared to the fiscal year ended September 30, 2009 as a result of slight decrease in server management and bandwidth leasing fees paid to third-party providers, share-based compensation expenses and tight control of our overall expenses. Our cost of services as a percentage of net revenues slightly decreased in the fiscal year ended September 30, 2011 as compared to the fiscal year ended September 30, 2010 as a result of relatively slower growth in salaries and related expenses, rental and related expenses, server management and bandwidth leasing fees paid to third-party providers, and share-based compensation expenses. Such slower growth was partially offset by the relatively higher growth in fees paid to our lecturers due to our expanded course offerings, more course production hours and higher hourly lecturer fees.

Historically, fees paid to lecturers to produce our courses constituted a large portion of our cost of services because we allocated significant resources to engage high-quality lecturers for our online courses and to increase the number of lecturers for our expanded course offerings. The number of lecturers actively producing online courses for us was 629, 370 and 325 in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. The decrease in the number of lecturers actively producing online courses for us in the fiscal year ended September 30, 2010 compared to the fiscal year ended September 30, 2009 resulted primarily from the overall decrease of renewal of our course offerings. In the fiscal year ended September 30, 2011, the number of lecturers decreased compared to the fiscal year ended September 30, 2010 primarily due to the adjustment and maintenance of a more qualified pool of lecturers. Leveraging the online medium, we are also achieving greater economies of scale as we are able to continuously increase our numbers of course participants without having to increase the number of our lecturers, which is a distinct advantage we enjoy over traditional offline schools and educational programs that are limited by traditional teacher-student classroom ratios. As a result, our fees paid to lecturers as a percentage of our net revenues decreased in the fiscal year ended September 30, 2010, as compared to the fiscal year ended September 30, 2009. However, our fees paid to lecturers as a percentage of our net revenues increased in the fiscal year ended September 30, 2011 as compared to the fiscal year ended September 30, 2010, primarily as a result of increase in hourly lecturer fees for our existing online course offerings and expansion of in-person accounting and healthcare professional training to the public.

Our service-oriented approach is a critical component of our online education business model. Accordingly, our tutors and course production technicians also play an important role in our delivery of quality services. While our lecturers primarily conduct lectures through pre-recorded audio-visual media, our tutors play a more immediate frontline role in the provision of our course services. They answer questions from course participants by email or by telephone, usually within a 24-hour time period. Delivering this level of quality service and responsiveness requires us to continuously maintain a large, well-trained pool of tutors to keep pace with the growth in the numbers of course enrollments, and to allocate sufficient resources to retain the top performing tutors to maintain the overall high-quality of our tutoring services. The number of our tutors decreased from 224 (including 91 part-time tutors) as of September 30, 2009 to 189 (including 81 part-time tutors) as of September 30, 2010, and increased to 192 (including 68 part-time tutors) as of September 30, 2011. To ensure a high quality learning experience, we also allocate resources to retain course production technicians capable of creating high quality audio-video course materials and other interactive features of our online courses. The number of our course production technicians decreased from 86 as of September 30, 2009 to 78 as of September 30, 2010 and increased to 85 as of September 30, 2011.

### ***Cost of Tangible Goods Sold***

Book sales costs comprise the cost of purchasing from third parties books that we re-sell, as well as fees we pay to third-party book printing companies to produce our proprietary books and reference materials and other fees related to content creation for our books and reference materials.

### **Operating Expenses**

Our operating expenses consist of selling expenses, general and administrative expenses, and impairment of purchased call option.

### ***Selling Expenses***

Selling expenses accounted for 22.3%, 22.0% (adjusted) and 23.5% of our net revenues in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. Our selling expenses consist primarily of advertising and promotion expenses, salaries and related expenses of our customer service staff and sales and marketing staff, commissions paid to our agents, freight and delivery expenses related to our books and reference materials, rental and related expenses of office facilities and other selling expenses. Our selling expenses comprised 22.3% of our net revenues in the fiscal year ended September 30, 2009 as we incurred significant share-based compensation expenses due to our share options granted in the fiscal year ended September 30, 2008, and repricing of our share options in the first quarter of the fiscal year ended September 30, 2009; incurred expenses relating to the acquired business start-up training business; higher salaries and welfare expenses as we added more personnel engaged primarily in customer service, and sales and marketing services; significant increase in advertising and promotional activities to promote our business and brand names; and significant increase in commissions paid to online agents due to an increase in the online sales of our courses. Our selling expenses as a percentage of net revenues decreased in 2010 due to a decrease in advertising and promotional activities as we exercised tight control of our overall expenses, partially offset by the higher salaries and welfare expenses in customer service and sales and marketing service and commissions paid to agents due to an increase in the sales of our courses. Our selling expenses increased to 23.5% of our net revenues in the fiscal year ended September 30, 2011 as a result of relatively higher growth in our advertising and promotional activities and commissions paid to agents due to an increase in the sales of our courses. Such higher growth was partially offset by the relatively lower growth in salaries and related expenses and share-based compensation expenses.

The aggregate amount of salaries paid to our customer service staff was significant as we maintained the number of our customer service staff at a high level with the increase in the number of course enrollments and other customers. In the future, as we seek to reduce our reliance on sales of our pre-paid study cards through third-party sales agents, we expect to increase the number of our customer service staff to increase the portion of sales of our products and services conducted directly through our own customer service staff.

The aggregate amount of salaries paid to our sales and marketing staff was also significant as we significantly increased the number of our sales and marketing staff to promote our business.

### ***General and Administrative Expenses***

Our general and administrative expenses accounted for 24.7%, 32.4% (adjusted) and 29.4% of our net revenues in the fiscal years ended September 30, 2009, 2010 and 2011, respectively. Our general and administrative expenses consist primarily of administrative staff compensation and benefits, professional fees, rental expenses, depreciation and amortization, and other miscellaneous expenses. Staff benefits include pension, medical insurance, unemployment insurance, work-related injury insurance and housing subsidies. Other miscellaneous expenses include travel, office, communication and entertainment expenses. Our general and administrative expenses was 24.7% of our net revenues in the fiscal year ended September 30, 2009 as we incurred significant share-based compensation expenses due to our share options granted and restricted shares issued in the fiscal year ended September 30, 2008, our share options granted to five non-executive directors in the first quarter of the fiscal year ended September 30, 2009, and repricing of our share options in the first quarter of the fiscal year ended September 30, 2009; expenses relating to the acquired business start-up training business; increased headcount for business expansion; and additional expenses associated with being a U.S. public company. Our general and administrative expenses increased to 32.4% (adjusted) of our net revenues in the fiscal year ended September 30, 2010 as compared to the fiscal year ended September 30, 2009 as we incurred additional share-based compensation expenses arising from our share options granted in the first quarter of the fiscal year ended September 30, 2010; made a significant bad debts provision for certain accounts receivables that have been outstanding for more than 360 days with respect to the business start-up training business, accounting continuing education courses and ITAT contest; increased headcount for business expansion; and additional professional expenses associated with being a U.S. public company. Our general and administrative expenses decreased to 29.4% of our net revenues in the fiscal year ended September 30, 2011 as compared to the fiscal year ended September 30, 2010 due to relatively lower growth in salaries and related expenses; decreased bad debts provision from \$2.2 million in the fiscal year ended September 30, 2010 to \$1.2 million in the fiscal year ended September 30, 2011. This slower growth was partially offset by the relatively significant growth in share-based compensation expenses arising from re-pricing and acceleration of the vesting of our share options granted under the Prior Plan in the fourth quarter of the fiscal year ended September 30, 2011. We expect that in connection with the expansion of our business, our general and administrative expenses will continue to increase as we hire additional personnel and incur additional costs.

### Share-based Compensation Expenses

We adopted our Share Incentive Plan, or the Prior Plan, on April 18, 2008. We adopted on July 2, 2008, and amended and restated on February 16, 2009, our 2008 Performance Incentive Plan, or the New Plan. An aggregate of 11,652,556 ordinary shares have been reserved for issuance under the Prior Plan. In addition, an aggregate of 11,267,992 ordinary shares have been reserved for issuance under the New Plan as of September 30, 2011. See “Item 6.B. Directors, Senior Management and Employees — Compensation — Share Options, Restricted Shares and Share Incentive Plans.” As of September 30, 2009, 2010 and 2011, there are outstanding options to purchase a total of 10,836,708, 11,620,104 and 12,488,012 ordinary shares, respectively, and as a result, we recorded share-based compensation expenses in the corresponding periods in connection with the options granted. In the fiscal years ended September 30, 2009 and 2011, we also recorded share-based compensation expenses in connection with restricted shares awarded to non-executive directors. In addition to re-pricing of all outstanding share options under the Prior Plan on December 2, 2008, we further reduced the exercise price of 8,066,700 and 1,398,300 outstanding share options under the Prior Plan from \$0.82 per share to \$0.615, which equaled the closing price of our ADSs on NYSE at the close of trading on September 27, 2011, and zero per share, respectively. Furthermore, the re-priced options had been accelerated to be fully vested on the same day. As a result, we further recorded incremental share-based compensation expenses in the fiscal year ended September 30, 2011. The amounts of these share-based compensation expenses are set forth below:

	For the Years Ended September 30,		
	2009	2010	2011
	\$	\$	\$
	(in thousands)		
<b>Share-based compensation expenses:</b>			
Restricted shares awarded to non-executive directors	16	—	104
Options granted to employees, non-employees and non-executive directors	3,904	4,387	5,920

As of September 30, 2009, 2010 and 2011, the unamortized compensation expenses in connection with our outstanding options were \$9.3 million, \$7.8 million and \$0.7 million, respectively.

### Impairment of goodwill, intangible assets and purchased call option

Zhengbao Yucai, which operates the business of start-up training services we acquired in March 2009, incurred net losses for the fiscal years of 2009 and 2010. In addition, in late 2009, we noted that Mr. Liang Ma, Yinglun Yucai, a company owned by Mr. Liang Ma, and Global Education Consortium Group Co., Limited, a company owned by Mr. Liang Ma’s wife, were engaged in competing businesses which is prohibited under the purchase agreement. As a result, we filed an arbitration application in January 2010 with the China International Economic and Trade Arbitration Commission, or CIETAC, against Mr. Liang Ma and the other related parties. Under these circumstances, we performed impairment tests for the goodwill, other intangible assets and the purchased call options acquired with the acquisition of the start-up training business as of September 30, 2010. Based on the impairment tests, there was no impairment of goodwill and other intangible assets as the start-up training business is expected to be profitable in the future. However, the option to acquire 49% equity interest of a company owned by Yinglun Yucai was fully impaired by US\$0.03 million and the option to acquire 30% equity interest in Zhengbao Yucai was impaired by US\$0.13 million. In June 2011, CIETAC, ruled, among other things, that Mr. Liang Ma shall surrender his 40% ownership interest in Zhengbao Yucai to us for no consideration. As a result, the option to acquire additional equity interest in Zhengbao Yucai of \$1.1 million was fully impaired in the fiscal year ended September 30, 2011. For more information on the arbitration, please see “Item 8. Financial Information — Legal Proceedings.” In September 2011, in conjunction with the discontinuance of operations of Champion Xinlixiang, we recorded an impairment loss of US\$2.1 million to write down the related carrying amounts of its assets to their fair values less cost to sell. Please see “—Loss from discontinued operations” for more information.

### Taxation

We are incorporated in the Cayman Islands. Under the current law of the Cayman Islands, we are not subject to income or capital gains tax. In addition, dividend payments are not subject to withholding tax in the Cayman Islands. However, there is a risk that we may be treated as resident in the PRC for tax purposes. See “Risk Factors — General Risks Relating to Conducting Business in China — Under China’s New EIT Law, we may be classified as a ‘resident enterprise’ of China. Such classification could result in unfavorable tax consequences to us and our non-PRC shareholders.”

CDEL Hong Kong was incorporated in Hong Kong and does not conduct any substantive operations of its own. No provision for Hong Kong profits tax has been made as CDEL Hong Kong has no assessable profits in Hong Kong in the fiscal years ended September 30, 2009, 2010 and 2011. In addition, no Hong Kong withholding tax will be imposed on any payments of dividends distributed by CDEL Hong Kong to us.

In February 2010, PENCIL was incorporated in Hong Kong as a wholly-owned subsidiary of CDEL Hong Kong. PENCIL has not conducted any substantive operations since its inception. No provision for Hong Kong profits tax has been made as PENCIL has no assessable profits in Hong Kong in the fiscal years ended September 30, 2010 and 2011. In addition, no Hong Kong withholding tax will be imposed on any payments of dividends distributed by PENCIL to us through CDEL Hong Kong.

### ***Enterprise Income Tax***

The current and deferred components of the income tax expense/(benefit) appearing in our consolidated statements of operations are as follows:

	Years ended September 30,		
	2009	2010 (adjusted)	2011
	\$	\$	\$
		(in thousands)	
Current tax expense	148	1,044	1,948
Deferred tax (expense)/benefit	1,330	(469)	(977)
	<u>1,478</u>	<u>575</u>	<u>971</u>

Champion Technology and Beijing Champion obtained tax preferential treatments as “high and new technology enterprises” or enjoyed a term tax holiday under New EIT Law that resulted in lower tax rates. Champion Technology is subject to the tax rate of 7.5% for 2009 and 15% for 2010 and 2011. Beijing Champion is subject to the tax rate of 15% from 2009 through 2011. Our other PRC entities are subject to standard income tax rate of 25% for 2009, 2010 and 2011. See “Risk Factors— General Risks Relating to Conducting Business in China — The discontinuation of any of the preferential tax treatments currently available to our PRC subsidiary, Champion Technology, and affiliated entity, Beijing Champion, could materially increase our tax liabilities.”

Our aggregated undistributed earnings of our subsidiaries located in the PRC that are available for distribution at September 30, 2011 are considered to be retained and indefinitely reinvested and accordingly, no provision has been made for the Chinese dividend withholding taxes that would be payable upon the distribution of those amounts to any entity within our group that is outside the PRC.

Under the Enterprise Income Tax Law, an enterprise established outside of the PRC with “de facto management bodies” within the PRC is considered a resident enterprise and will be subject to the enterprise income tax at the rate of 25% on its global income. The implementation rules define the term “de facto management bodies” as establishments that carry out substantial and overall management and control over the manufacturing and business operations, personnel, accounting, properties, etc. of an enterprise. The SAT issued the Notice Regarding the Determination of Chinese-Controlled Offshore Incorporated Enterprises as PRC Tax Resident Enterprises on the Basis of De Facto Management Bodies, or Circular 82, on April 22, 2009. Circular 82 provides certain specific criteria for determining whether the “de facto management body” of a Chinese-controlled offshore-incorporated enterprise is located in China. In addition, the SAT issued a bulletin on August 3, 2011, effective September 1, 2011, providing more guidance on the implementation of Circular 82. This bulletin clarifies matters including residence status determination, post-determination administration and competent tax authorities. Although both Circular 82 and the bulletin only apply to offshore enterprises controlled by PRC enterprises and not those controlled by PRC individuals, the determination criteria set forth in Circular 82 and the bulletin may reflect the SAT’s general position on how the “de facto management body” test should be applied in determining the tax residency status of offshore enterprises and how the administration measures should be implemented with respect to such enterprises, regardless of whether they are controlled by PRC enterprises or PRC individuals. Although we do not believe that our legal entities organized outside of the PRC constitute PRC resident enterprises, it is possible that the PRC tax authorities could reach a different conclusion. See “Risk Factors—Risks Relating to Doing Business in China— Under the PRC enterprise income tax law, we may be classified as a PRC ‘resident enterprise’, which could result in unfavorable tax consequences to us and our shareholders and have a material adverse effect on our results of operations and the value of your investment.”

### ***Business Tax and Related Surcharges***

We are subject to approximately 3.3% business tax and related surcharges on the revenues earned from provision of online education services, which are recognized net of all business tax and related surcharges. Our other services related revenues are subject to 3.3% to 5.5% business tax and related surcharges, which are also recognized net of all business tax and related surcharges. Such business tax and related surcharges net against revenues for the years ended September 30, 2009, 2010 and 2011 are approximately \$1.0 million, \$1.1 million and \$1.3 million, respectively. In addition, we are subject to 5% (or 5.5% after December 1, 2010) business tax and related surcharges on service fee received by Champion Technology and Champion Education Technology from Beijing Champion, which tax and surcharges are included in the cost of services.

### ***Value Added Tax***

In accordance with the relevant tax laws in the PRC, value-added tax, or VAT, is calculated based on the sales value of books and reference materials and is payable by the purchaser. Revenues are recognized net of all VAT imposed by governmental authorities and collected from customers concurrent with revenue-producing transactions. VAT related to our books and reference materials sales amounted to approximately \$0.4 million, \$0.5 million and \$0.6 million for the fiscal years ended September 30, 2009, 2010 and 2011, respectively. We are required to remit the VAT we collected to the tax authority, but may deduct the VAT we have paid on eligible purchases. To the extent that we paid more VAT than collected, the difference represents the net VAT recoverable balance at the balance sheet date. As of September 30, 2010 and 2011, there was no such VAT recoverable balance in our consolidated financial statements.

## **Loss from discontinued operations**

Champion Xinlixiang, which operated our Gaokao retake preparation and high-school supplementary tutoring business that we acquired in September 2009 from Mr. Junnan Ye and Mr. Xiujie Hu, incurred significant operating loss in the fiscal year ended September 30, 2011. As a result, we decided to discontinue such business and put the related assets and business up for sale. Prior year financial statements for the fiscal years of 2009 and 2010 have been adjusted to present the operations of Champion Xinlixiang as a discontinued operation.

The goodwill and non-compete agreement related to Champion Xinlixiang were impaired by \$1.4 million and \$0.3 million, respectively, for the fiscal year ended September 30, 2010. In the fiscal year ended September 30, 2011, the related goodwill, property, plant and equipment, and non-compete agreement were further written down by \$0.8 million, \$1.0 million and \$0.3 million, respectively, to write down the related carrying amounts to their fair values less cost to sell. The revenue and pretax loss from the discontinued operations included in our consolidated statement of operations were \$2.2 million and \$2.2 million, respectively, for the year ended September 30, 2010 and \$1.8 million and \$3.4 million, respectively, for the year ended September 30, 2011.

## **Critical Accounting Policies**

We prepare our consolidated financial statements in conformity with U.S. GAAP, which requires us to make judgments, estimates and assumptions that affect the reported amounts of our assets and liabilities, disclosure of contingent assets and liabilities on the date of each set of consolidated financial statements and the reported amounts of revenues and expenses during each financial reporting period. We continually evaluate these estimates and assumptions based on the most recently available information, our own historical experience and various other assumptions that we believe to be reasonable under the circumstances. Since the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates as a result of changes in our estimates or changes in the facts or circumstances underlying our estimates and assumptions.

An accounting policy is considered to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time such estimate is made, and if different accounting estimates that reasonably could have been used, or changes in the accounting estimates that are reasonably likely to occur periodically, could materially impact the consolidated financial statements. Some of our accounting policies require higher degrees of judgment than others in their application. We consider the policies discussed below to be critical to an understanding of our consolidated financial statements as their application places the most significant demands on our judgment. When reviewing our consolidated financial statements, you should take into account:

- our critical accounting policies discussed below;
- the related judgments made by us and other uncertainties affecting the application of these policies;
- the sensitivity of our reported results to changes in prevailing facts and circumstances and our related estimates and assumptions; and
- the risks and uncertainties described under “Item 3.D. Key Information — Risk Factors.”

See Note 2 to our audited consolidated financial statements included in this annual report for additional information regarding our significant accounting policies.

### ***Revenue Recognition***

We recognize revenues from our services and sales of products when the following four criteria are met: (i) persuasive evidence of an arrangement exists, (ii) the service has been rendered, (iii) the fees are fixed or determinable, and (iv) collectability is reasonably assured.

*Online education services.* We generate most of our revenues from online education services provided to course participants pursuant to two types of revenue models — a non-refundable course model and a refundable course model.

For online courses using the non-refundable course model, we recognize revenues on a straight line basis over the subscription period from the customers’ enrollment in the courses to the end of courses. For online courses using the refundable course model, if the customers complete the courses and fail the professional exams and their scores are within a range provided for in the agreement, we offer the customers either a full refund or the right to retake the course. The customers must notify us within a 15-day period after the professional examinations scores are released in order to be eligible for the refund or the right to retake the course. The proceeds from the refundable course model are initially recorded as “refundable fees”. We recognize such revenues upon the expiration of the customers’ right to either receive a refund or ratably over the course period if the customers decide to retake the course before the expiration of such right.

Customers enroll for online courses mainly through the use of prepaid study cards which are purchased from distributors. We sell to our distributors prepaid study cards at a discount to the face value of the cards. We recognize the after-discount-selling-price as revenue over the period the online course is available to the customer, which generally is from the enrollment date to the completion of the relevant professional examination date. For prepaid study cards that are not activated for course enrollment, we recognize revenues upon expiration of the cards. Prepaid study cards that have been activated but have not been used to enroll online courses do not have an expiry date and, therefore, the related revenues will be deferred until they are used to enroll in online courses. Customers who enroll with us directly are eligible to a refund within a seven-day trial period. Accordingly, revenue recognition would not start prior to the lapse of the seven-day trial period.

We may, at times, offer volume discounts to our distributors for purchases over a specified amount of prepaid cards during a specified period of time, generally one year. Because we cannot reasonably estimate the amount of future rebates relating to these volume discounts, we record a deferred revenue balance for the maximum potential amount of volume discount. If the number of purchases specified in the volume discount provisions is not reached upon the expiry of the volume discount period, we then recognize the deferred revenue relating to such volume discount for each study card as revenue over the remaining period that the online course is available to the user who enrolls using the study card or immediately if the related online course has been completed. Additionally, we recognize proceeds allocated to the rebate study cards that have never been activated for course enrollment as revenues upon expiration of the cards.

*Books and reference materials.* We sell books and reference materials to end users directly or through distributors. Revenues relating to such sales are deferred until cash is collected. Inventory costs of products delivered to distributors for which revenues have been deferred are presented as “deferred costs” on the consolidated balance sheets.

We also sell books and reference materials together with study cards which allow the customers to take a certain number of on-line courses for no additional charge. These sales are considered arrangements with two deliverables, consisting of the delivery of books and reference material and the on-line courses service.

In October 2009, the FASB published FASB ASU 2009-13, Revenue Recognition (Topic 605)—Multiple-Deliverable Revenue Arrangements. ASU 2009-13 addresses the accounting for multiple-deliverable arrangements to enable vendors to account for products or services (deliverables) separately rather than as a combined unit. Specifically, this guidance amends the criteria in ASC Subtopic 605-25, Revenue Recognition-Multiple-Element Arrangements, for separating consideration in multiple-deliverable arrangements. This guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence if available (“VSOE”); (b) third-party evidence (“TPE”) if vendor-specific objective is not available; or (c) estimated selling price (“ESP”) if neither vendor-specific objective evidence nor third-party evidence is available. In addition, this guidance significantly expands required disclosures related to a vendor’s multiple-deliverable revenue arrangements. The provisions of ASU 2009-13 are effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Early adoption is permitted.

We prospectively adopted ASU 2009-13 to revenue arrangements containing multiple deliverables that were entered into on or after October 1, 2010. As neither VSOE nor TPE of the deliverables exist due to the significant variability in the prices charged, we allocate revenues to each deliverable based on their relative selling prices. When ESP is used, we determine the best estimate of selling price by applying the same pricing policies and methodologies that would be used to determine the price to sell the deliverable on a standalone basis. We recognize revenues of book and material sales when cash is collected and revenues of the study card over the subscription period the online course is available to end users who enroll using the study cards or upon expiration of the study cards. Prior to the adoption of this new guidance, we concluded that sales of books and reference material in these multiple-element arrangements cannot be accounted for as a separate accounting unit due to a lack of VSOE of the undelivered on-line courses, and accordingly we recognize the entire revenue over the subscription period that the online course is available to end users who enroll using the study cards or upon expiration of the study cards.

The adoption of ASU 2009-13 did not have a significant effect on our consolidated financial position or results of operations.

*Others.* We derive other revenue from provision of offline education services, courseware production services, platform production services, and others.

We recognize revenues from offline training when the training courses are provided. For offline training sponsored by government authorities, the tuition fees of the training participants are subsidized by the government. We are not able to determine the enrollment and fees to be earned until such figures are confirmed by government agencies after the completion of services. Therefore, we recognize revenues from such services upon cash receipt or the receipt of confirmation from government authorities, whichever is earlier.

We recognize revenues from sales of courseware or platforms, which are designed and developed pursuant to the requests from customers, when the courseware or platforms are accepted by the customers. We have no significant remaining obligation with respect to the courseware or platforms upon the acceptance of the customers.



From time to time, we also enter into arrangement to provide the development and maintenance of online platforms to our customers. The on-line platforms enable customers to sell products through our website. After the development of online platforms, we provide support and maintenance services, which encompass bug fixes and general technical support but do not include upgrades or increased functionality of the online platform, for a period of time for no additional charge. The development of online platform and the support and maintenance services have never been sold separately and they do not have standalone value to the customers. Accordingly, we account for such arrangement as a single unit of accounting and recognize revenues ratably over the support and maintenance services period.

We recognize revenues from other services, including magazine content production, advertising and consulting services, over the period when such services are provided.

#### ***Long-Lived Assets — Property, Plant and Equipment and Intangible Assets***

Judgment is required to determine the estimated useful lives of our long-lived assets. Changes in these estimates and assumptions could materially impact our financial position and results of operations.

We evaluate our long-lived assets or asset group including intangibles with finite lives for impairment whenever events or changes in circumstances (such as a significant adverse change to market conditions that will impact the future use of the assets) indicate that the carrying amount of a group of long-lived assets may not be fully recoverable. When these events occur, we evaluate the impairment by comparing the carrying amount of the assets to future undiscounted net cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected undiscounted cash flows is less than the carrying amount of the assets, we recognize an impairment loss based on the excess of the carrying amount of the asset group over its fair value, generally based upon discounted cash flows.

We performed the impairment tests for intangible assets acquired with the acquisitions of Zhengbao Yucai and Champion Xinlixiang as of September 30, 2010 because both entities performed below expectations. We also performed the impairment tests for property, plant and equipment and intangible assets acquired with the acquisition of Champion Xinlixiang as of September 30, 2011 as we decided to discontinue the related business. For purposes of the recognition and measurement of an impairment loss of property, plant and equipment, and intangible assets, the reporting unit, as noted below, is considered the lowest level asset group that generates identifiable independent cash flows. Because the sum of undiscounted future cash flows expected to generate from the use and eventual disposition of the business start-up training service exceeded its carrying amount, no impairment of intangible assets of Zhengbao Yucai was identified as of September 30, 2010. However, the non-compete agreement relating to Champion Xinlixiang was impaired by US\$0.3 million. As of September 30, 2011, the property, plant and equipment, and non-compete agreement relating to Champion Xinlixiang was further impaired by \$1.0 million and \$0.3 million, respectively. If different judgments or estimates had been utilized, material differences could have resulted in the amount and timing of any impairment charge and the related depreciation and amortization charges.

#### ***Goodwill***

Goodwill represents the cost of an acquired business in excess of the fair value of identifiable tangible and intangible net assets purchased. We assign all the assets and liabilities of an acquired business, including goodwill, to reporting units. We perform our goodwill impairment test on September 30th of each year. Impairment is tested using a two-step process. The first step compares the fair value of each reporting unit to its carrying amount, including goodwill. As of September 30, 2011, we had three reporting units: online education service, business start-up training service and Gaokao retake business. We are in the process of disposing Gaokao retake business, please see “— Description of Key Line Items — Loss from discontinued operations” for more information.

If the fair value of a reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step will not be required. If the carrying amount of a reporting unit exceeds its fair value, the second step compares the implied fair value of goodwill to the carrying value of a reporting unit's goodwill. The implied fair value of goodwill is determined in a manner similar to accounting for a business combination with the allocation of the assessed fair value determined in the first step to the assets and liabilities of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized for any excess in the carrying value of goodwill over the implied fair value of goodwill. Estimating fair value is performed by utilizing various valuation techniques.

The following table sets forth the details of goodwill impairment test as of September 30, 2011:

	<u>Online education service</u>	<u>Business start-up training service</u> (in thousands of \$)	<u>Gaokao retake preparation and high-school supplementary tutoring business – discontinued operation</u>	<u>Total</u>
Estimated fair value	83,215	3,297	641	87,153
Carrying value net	28,215	2,771	1,207	32,193
Percentage by which the fair value exceed or below the carrying value	194.9%	19.0%	(46.9)%	
The estimated fair value of goodwill allocated to the reporting unit	*	*	0	
The carrying value of goodwill	5,642	1,761	764	8,167
Foreign currency adjustment	*	*	(6)	(6)
Goodwill impairment loss	*	*	(758)	(758)

\* The second step of goodwill impairment test was not performed for the reporting units of online education service and business start-up training service.

In determining the fair values of our reporting units as of September 30, 2011, we considered the discounted cash flow method, or DCF, of the income approach to be more reliable than other approaches. The discounted cash flow for each reporting unit was projected based on financial forecast developed by management for planning purposes. Cash flows beyond the forecast periods were estimated using a terminal value calculation, which incorporated historical and forecasted financial trends for each reporting unit. Specifically, the income approach valuation included a cash flow discount rate at 15% - 33.5% and a terminal value growth rate at 3%. Publicly available information regarding the market capitalization of the Group was also considered in assessing the reasonableness of the aggregate fair value of all the reporting units estimated using the income approach valuation methodology. Based on the result of goodwill impairment test as of September 30, 2011, an impairment loss of US\$0.8 million was recorded for the goodwill related to Gaokao retake preparation and high-school supplementary tutoring business and no impairment of goodwill was identified for the reporting units of online education service and business start-up training service.

The valuations are based on information available as of the impairment review date and are based on expectations and assumptions that have been deemed reasonable by the management. Any changes in key assumptions, including unanticipated events and circumstances, may affect the accuracy or validity of such estimates and could potentially result in additional impairment charge.

### *Income taxes*

We follow the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial reporting and tax bases of assets and liabilities using enacted tax rates that will be in effect in the period in which the differences are expected to reverse. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes. The effect on deferred taxes of a change in tax rates is recognized in our income statement in the period that includes the enactment date. We consider current tax laws and our interpretation of them when we make our judgments, assumptions and estimates relative to current provision for income tax. We also assess a valuation allowance to offset deferred tax assets if based on the weight of available evidence, it is more likely than-not that some portion, or all, of the deferred tax assets will not be realized. Such evidence includes our estimates of future taxable income and tax planning strategies. Changes in relevant tax laws, and our judgments, assumptions and estimates relative to current provision for income tax could have resulted in material differences in the amount of income taxes provided in our consolidated financial statements.

Effective October 1, 2007, we adopted the recognition and measurement methods under the authoritative interpretation regarding the accounting and disclosure for uncertainty in tax positions. The guidance requires that we recognize the impact of a tax position in the financial statements if that position is more likely than not of being sustained upon audit by the tax authority, based on the technical merits of the position. The amount recognized is measured as the largest amount of benefit that is more likely than not of being realized upon ultimate settlement. Based on this assessment, as of September 30, 2009, 2010 and 2011, respectively, we have recognized an approximately \$0.2 million, \$0.2 million and \$0.2 million accrual for unrecognized tax benefits which is included in the account of "accrued expenses and other liabilities". The final outcome of the tax uncertainty is dependent upon various matters including tax examinations, interpretation of tax laws or expiration of statutes of limitation. We recognize, if any, interest related to unrecognized tax benefit in interest expense and penalties in other expenses. Changes in relevant tax laws, and our judgments, assumptions and estimates relative to current provision for income tax could have resulted in material differences in the amount of income taxes provided in our consolidated financial statements.

Uncertainties exist with respect to how PRC's New EIT Law applies to our overall operations, and more specifically, with regard to our tax residency status. The New EIT Law includes a provision specifying that legal entities organized outside of the PRC will be considered residents for PRC income tax purposes if their place of effective management or control is within the PRC. The implementation rules to the New EIT Law provide that non-resident legal entities will be considered PRC residents if substantial and overall management and control over the manufacturing and business operations, personnel, accounting, properties, among others, occur within the PRC. Despite the present uncertainties resulting from the limited PRC tax guidance on the issue, we do not believe that our legal entities organized outside of the PRC should be treated as residents for the Enterprise Income Tax Law's purposes. If one or more of our legal entities organized outside of the PRC were characterized as PRC tax residents, the impact would adversely affect our results of operation. See "Item 3.D. Key Information — Risk Factors — General Risks Relating to Conducting Business in China— Under China's New EIT Law, we may be classified as a "resident enterprise" of China. Such classification could result in unfavorable tax consequences to us and our non-PRC shareholders."

### ***Inventory Obsolescence***

We evaluate our inventory for impairment on a quarterly or more frequent basis whenever events or changes in circumstances — such as the levels of inventory versus customer requirements and obsolescence, the product life cycle status, and the aging analysis of the inventory — indicate that the carrying amount of inventories may not be fully recoverable. The evaluation also involves consideration of the market prices of inventories. At each balance sheet date, we identify inventories that are worth less than cost and write them down to lower of cost or market prices and the difference is expensed to our cost of sales for that period. Although we consider such write-down of inventories to be adequate and proper, different judgments or estimates could have resulted material differences in the amount and timing of any write-downs and the related amount expensed to our cost of sales.

### ***Share-based Compensation Expenses***

In the fiscal years ended September 30, 2009, 2010 and 2011, we granted to our non-executive directors and employees share-based compensation awards subject to various graded vesting under the New Plan. In addition to re-pricing all outstanding share options under the Prior Plan on December 2, 2008, we further reduced the exercise price of 8,066,700 and 1,398,300 outstanding share options under the Prior Plan from \$0.82 per share to \$0.615, which equaled the closing price of our ADSs on NYSE on September 27, 2011, and zero per share, respectively. Furthermore, the re-priced options had been accelerated to be fully vested on the same day.

Share-based payment transactions with employees and non-executive directors are measured based on the grant-date fair value of the equity instrument issued and recognized as compensation expense over the requisite service period, with a corresponding addition to paid-in capital. We recognize compensation expense over the vesting term on a straight-line basis with the amount of compensation expense recognized during any period not less than the portion of the grant-date value of the option vested during that period.

Share-based payment transactions with non-employees are measured based on the fair value at the earlier of the commitment date or the date at which the non-employee's performance is complete. We recognize compensation expense using the graded vesting attribution method.

In addition, the total incremental compensation expense resulting from the modifications of the exercise price and vesting period of all outstanding share options under the Prior Plan is recognized over the remaining requisite service period for such employees and non-employees, respectively.

We estimated the fair value of each option award granted to employees, and non-employees under the Prior Plan using the Black-Scholes Option Pricing Model. We also estimated the fair value of each option award granted to non-executive directors and employees under the New Plan using the Black-Scholes Option Pricing Model. The volatility assumption was estimated based on the price volatility of the shares of education companies that are publicly traded on securities markets in the United States and selected by us as guideline companies because we did not have sufficient historical data to calculate expected volatility of the price of the underlying ordinary shares over the expected term of the options. The expected term was estimated based on the vesting, contractual terms and our expectation of exercise behavior of the option grantees. The risk-free rate was based on the market yield of China Sovereign Bonds denominated in US\$ with maturity terms equal to the expected term of the option awards. Prior to the completion of initial public offering in July 2008, when estimating the fair value of the ordinary shares on the grant date, we considered a number of factors, including our financial condition, financial and operating prospects with reference to our equity transactions at that time. After our initial public offering, the closing market price of our ordinary shares on the grant date or measurement date was used as the fair value of our ordinary shares on that date.

We estimated forfeitures at the time of grant based on our historical experiences and record share-based compensation expenses only for those awards that are expected to vest. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods.

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

In May 2011, the Financial Accounting Standard Board (“FASB”) issued an authoritative pronouncement on fair value measurement. The guidance is the result of joint efforts by the FASB and International Accounting Standards Board to develop a single, converged fair value framework. The guidance is largely consistent with existing fair value measurement principles in U.S. GAAP. The guidance expands the existing disclosure requirements for fair value measurements and makes other amendments, mainly including:

- Highest-and-best-use and valuation-premise concepts for non-financial assets – the guidance indicates that the highest-and-best-use and valuation-premise concepts only apply to measuring the fair value of non-financial assets.
- Application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk – the guidance permits an exception to fair value measurement principles for financial assets and financial liabilities (and derivatives) with offsetting positions in market risks or counterparty credit risk when several criteria are met. When the criteria are met, an entity can measure the fair value of the net risk position.
- Premiums or discounts in fair value measure – the guidance provides that premiums or discounts that reflect size as a characteristic of the reporting entity’s holding (specifically, a blockage factor that adjusts the quoted price of an asset or a liability because the market’s normal daily trading volume is not sufficient to absorb the quantity held by the entity) rather than as a characteristic of the asset or liability (for example, a control premium when measuring the fair value of a controlling interest) are not permitted in a fair value measurement.
- Fair value of an instrument classified in a reporting entity’s stockholders’ equity – the guidance prescribes a model for measuring the fair value of an instrument classified in stockholders’ equity; this model is consistent with the guidance on measuring the fair value of liabilities.
- Disclosures about fair value measurements –the guidance expands disclosure requirements, particularly for Level 3 inputs. Required disclosures include:

(i) For fair value measurements categorized in Level 3 of the fair value hierarchy: (1) a quantitative disclosure of the unobservable inputs and assumptions used in the measurement, (2) a description of the valuation process in place (e.g., how the entity decides its valuation policies and procedures, as well as changes in its analyses of fair value measurements, from period to period), and (3) a narrative description of the sensitivity of the fair value to changes in unobservable inputs and interrelationships between those inputs.

(ii) The level in the fair value hierarchy of items that are not measured at fair value in the statement of financial position but whose fair value must be disclosed.

The guidance is to be applied prospectively and is effective for interim and annual periods beginning after December 15, 2011, for public entities. Early application by public entities is not permitted. We do not expect the adoption of this guidance to have a significant effect on our consolidated financial statements.

In June 2011, the FASB issued an authoritative pronouncement to require an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both cases, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders’ equity. The guidance does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The guidance should be applied retrospectively. For public entities, the guidance is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. In December 2011, the FASB issued an authoritative pronouncement entitled “Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update.” This guidance allows the FASB to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the FASB is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report reclassifications out of accumulated other comprehensive income, consistent with the presentation requirements in effect before update the pronouncement issued in June 2011. We do not expect the adoption of this guidance to have a significant effect on our consolidated financial statements.

In September 2011, the FASB issued an authoritative pronouncement related to testing goodwill for impairment. The guidance is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. The guidance permits an entity to first assess qualitative factors to determine whether it is “more likely than not” that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if a public entity’s financial statements for the most recent annual or interim period have not yet been issued. We do not expect the adoption of this pronouncement to have a significant impact on our financial condition or results of operations.

In December 2011, the FASB issued an authoritative pronouncement related to Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update. This guidance allows the FASB to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the FASB is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before update the pronouncement issued in June 2011. We do not expect the adoption of this guidance to have a significant effect on its consolidated financial statements.

In December 2011, the FASB has issued an authoritative pronouncement entitled “Disclosures about Offsetting Assets and Liabilities.” The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. We do not expect the adoption of this pronouncement to have a significant impact on our financial condition or results of operations.

## Results of Operations

The following table sets forth a summary, for the periods indicated, of our consolidated results of operations and each item expressed as a percentage of our total net revenues. Our historical results presented below are not necessarily indicative of the results that may be expected for any future period.

	Years Ended September 30,					
	2009 (adjusted)(1)		2010(adjusted)(1)		2011(1)	
	\$	% of net revenues	\$	% of net revenues	\$	% of net revenues
	(In thousands, except for percentages)					
<b>Net Revenues</b>						
Online education services	22,279	74.0%	23,982	73.6%	30,788	74.1%
Books and reference materials	2,709	9.0%	3,939	12.1%	4,743	11.4%
Others	5,133	17.0%	4,658	14.3%	6,033	14.5%
<b>Total net revenues</b>	<b>30,121</b>	<b>100.0%</b>	<b>32,579</b>	<b>100.0%</b>	<b>41,564</b>	<b>100.0%</b>
<b>Cost of sales:</b>						
Cost of services	(12,834)	(42.6)%	(13,283)	(40.8)%	(16,840)	(40.5)%
Cost of tangible goods sold	(1,577)	(5.2)%	(2,070)	(6.3)%	(2,794)	(6.7)%
<b>Total cost of sales</b>	<b>(14,411)</b>	<b>(47.8)%</b>	<b>(15,353)</b>	<b>(47.1)%</b>	<b>(19,634)</b>	<b>(47.2)%</b>
<b>Gross profit</b>	<b>15,710</b>	<b>52.2%</b>	<b>17,226</b>	<b>52.9%</b>	<b>21,930</b>	<b>52.8%</b>
<b>Operating expenses:</b>						
Selling expenses	(6,722)	(22.3)%	(7,176)	(22.0)%	(9,771)	(23.5)%
General and administrative expenses	(7,432)	(24.7)%	(10,535)	(32.4)%	(12,221)	(29.4)%
Impairment of purchased call options	—	— %	(162)	(0.5)%	(1,115)	(2.7)%
<b>Total operating expenses</b>	<b>(14,154)</b>	<b>(47.0)%</b>	<b>(17,873)</b>	<b>(54.9)%</b>	<b>(23,107)</b>	<b>(55.6)%</b>
Other operating income	292	0.9%	74	0.2%	603	1.5%
<b>Operating (loss) income</b>	<b>1,848</b>	<b>6.1%</b>	<b>(573)</b>	<b>(1.8)%</b>	<b>(574)</b>	<b>(1.3)%</b>
Interest income	740	2.5%	458	1.4%	883	2.1%
Exchange loss	(6)	(0.0)%	(66)	(0.2)%	(143)	(0.3)%
<b>Income (loss) before income taxes</b>	<b>2,582</b>	<b>8.6%</b>	<b>(181)</b>	<b>(0.6)%</b>	<b>166</b>	<b>0.5%</b>
Less: Income tax expense	(1,478)	(4.9)%	(575)	(1.8)%	(971)	(2.3)%
<b>Net (loss) income from continuing operations</b>	<b>1,104</b>	<b>3.7%</b>	<b>(756)</b>	<b>(2.4)%</b>	<b>(805)</b>	<b>(1.8)%</b>
Net loss of continuing operations attributable to noncontrolling interest	82	0.2%	911	2.8%	303	0.7%
Net (loss) income from continuing operations attributable to						

China Distance Education Holdings Limited	1,186	3.9%	155	0.4%	(502)	(1.1)%
Net (loss) income from discontinued operations attributable to China Distance Education Holdings Limited, net of tax	<u>2</u>	<u>0.0%</u>	<u>(2,053)</u>	<u>(6.2)%</u>	<u>(3,300)</u>	<u>(8.0)%</u>
<b>Net (loss) income attributable to China Distance Education Holdings Limited</b>	<u><u>1,188</u></u>	<u><u>3.9%</u></u>	<u><u>(1,898)</u></u>	<u><u>(5.8)%</u></u>	<u><u>(3,802)</u></u>	<u><u>(9.1)%</u></u>

- (1) The selected consolidated statements of operations data for the fiscal years ended September 30, 2009, 2010 and 2011 have reflected the adoption of ASC Topic 810-10-65. In addition, the selected consolidated statements of operations data for the fiscal years ended September 30, 2009 and 2010 have been retrospective adjusted to reflect the effect of the discontinued operations, where applicable.

## **Fiscal Year Ended September 30, 2011 Compared to Fiscal Year Ended September 30, 2010**

### ***Net Revenues***

Our total net revenues increased by 27.6% to \$41.6 million in the fiscal year ended September 30, 2011 from \$32.6 million (adjusted) in the fiscal year ended September 30, 2010, as a result of growth in sales of our online education services, books and reference materials, and other products and services.

*Online education services.* Net revenues from our online education services increased by 28.4% to \$30.8 million in the fiscal year ended September 30, 2011 from \$24.0 million in the fiscal year ended September 30, 2010. This increase was primarily due to overall growth in the total number of our online course enrollments to 1,578,000 in the fiscal year ended September 30, 2011 from over 1,211,000 in the fiscal year ended September 30, 2010. Our accounting courses continued to account for the majority of our course enrollments with a total enrollment of approximately 1,320,000 in the fiscal year ended September 30, 2011 while enrollments in our self-taught study process monitoring programs for self-taught learners and our healthcare and construction engineering courses also increased. Of this revenue increase, our Accounting Professional Qualification Examination courses, CPA Qualification Examination courses, Elementary, Intermediate and Advanced Level Accounting Professional Qualification Examinations courses, courses to self-taught learners, construction engineering courses, and healthcare courses generated revenues of approximately \$1.3 million, \$5.0 million, \$7.8 million, \$1.2 million, \$1.9 million, and \$4.6 million, respectively, in the fiscal year ended September 30, 2011. Our revenue growth rate in the fiscal year ended September 30, 2011 was partially impacted by the overall decrease in enrollment of our CPA Qualification Examination courses, and Elementary, Intermediate and Advanced Level Accounting Professional Qualification Examinations courses from approximately 120,000 and 216,000 in the fiscal year ended September 30, 2010 to approximately 111,000 and 193,000, respectively in the fiscal year ended September 30, 2011.

*Books and reference materials.* Net revenues from our sales of books and reference materials increased by 20.4% to \$4.7 million in the fiscal year ended September 30, 2011 from \$3.9 million in the fiscal year ended September 30, 2010. The increase in our books and reference materials revenues was due primarily to an overall increase in books and reference materials sales.

*Others.* Our other net revenues increased to \$6.0 million in the fiscal year ended September 30, 2011 from \$4.7 million (adjusted) in the fiscal year ended September 30, 2010, primarily due to revenues generated from business start-up training courses and primary and secondary school supplementary courses. Our other revenue growth rate in the fiscal year ended September 30, 2011 was partially impacted by the decrease in revenues of our platform production services, course production services, and information technology related services. Other revenues also included sales of magazine content production services, tax and accounting related services through our [www.chinaacc.com](http://www.chinaacc.com) website, in-person accounting and healthcare professional training to accounting firms and the general public, and, to a lesser extent, other value-added services offered through our websites.

### ***Gross Profit***

Our gross profit increased by 27.3% to \$21.9 million in the fiscal year ended September 30, 2011 from \$17.2 million (adjusted) in the fiscal year ended September 30, 2010. Our gross margin decreased slightly to 52.8% in the fiscal year ended September 30, 2011 from 52.9% (adjusted) in the fiscal year ended September 30, 2010. The decrease in gross margin was primarily driven by the relatively significant growth in fees paid to our lecturers due to our expanded course offerings, increase in hourly lecturer fees for existing online course offerings and expansion of in-person accounting and healthcare professional training to the public. The impact was partially offset by relative low growth in salaries and related expenses, rental and related expenses, server management and bandwidth leasing fees paid to third-party providers, share-based compensation expenses, and revenue increase in our product mix of the higher margin books and reference materials.

### ***Operating Expenses***

Our operating expenses increased by 29.3% to \$23.1 million in the fiscal year ended September 30, 2011 from \$17.9 million (adjusted) in the fiscal year ended September 30, 2010, primarily as a result of additional share-based compensation expenses arising from the re-pricing and acceleration of the vesting of our share options granted under the Prior Plan in the fourth quarter of the fiscal year ended September 30, 2011, impairment of purchased call option acquired with the acquisition of Zhengbao Yucai, significant increase in advertising and promotional activities, and significant increase in commissions paid to agents. Such increase was partially offset by the relatively slower growth in overall salaries and related expenses and decreased bad debts provision.

*Selling expenses.* Our selling expenses increased by 36.2% to \$9.8 million in the fiscal year ended September 30, 2011 from \$7.2 million (adjusted) in the fiscal year ended September 30, 2010. This increase resulted primarily from significant increase in advertising and promotional activities to promote our business and brand names, significant increase in commissions paid to agents due to an increase in the sales of our courses, and higher salaries and welfare expenses in sales and marketing service as we significantly increased our sales and marketing staff to promote our business.

*General and administrative expenses.* Our general and administrative expenses increased by 16.0% to \$12.2 million in the fiscal year ended September 30, 2011 from \$10.5 million (adjusted) in the fiscal year ended September 30, 2010. This increase was primarily due to \$3.3 million of share-based compensation expenses we incurred in the fiscal year ended September 30, 2011. This was offset by the decrease in bad debts provision made for certain accounts receivables that have been outstanding for more than 360 days from \$2.2 million in the fiscal year ended September 30, 2010 to \$1.2 million in the fiscal year ended September 30, 2011. Our administrative staff salaries and related expenses increased to \$2.9 million. Our professional fees increased to \$2.2 million. Some of our other components of general and administrative expenses also increased due to the expansion of our business.

*Impairment of purchased call option.* Zhengbao Yucai, which operates the business of start-up training services that we acquired in March 2009, incurred net losses for the fiscal years of 2009 and 2010. In addition, in late 2009, we noted that Mr. Liang Ma, Yinglun Yucai, a company owned by Mr. Liang Ma, and Global Education Consortium Group Co., Limited, a company owned by Mr. Liang Ma's wife, engaged in competing businesses, which is prohibited under the purchase agreement. As a result, we filed an arbitration application in January 2010 with the China International Economic and Trade Arbitration Commission, or CIETAC, against Mr. Liang Ma and the other related parties. In June 2011, CIETAC, ruled, among other things, that Mr. Liang Ma shall surrender his 40% ownership interest in Zhengbao Yucai to us for no consideration. As a result, the option to acquire additional equity interest in Zhengbao Yucai of \$1.1 million was fully impaired in the fiscal year ended September 30, 2011. For more information about the arbitration, please see "Item 8. Financial Information-Legal Proceedings."

### ***Other Operating Income***

In the fiscal year ended September 30, 2011, we had other operating income of \$0.6 million which mainly was compensation we received from Mr. Liang Ma under the arbitral awards from CIETAC in June 2011. In the fiscal year ended September 30, 2010, we had other operating income of \$0.07 million which was a one-time subsidy we received from the Beijing Haidian District Bureau of Finance for one of our trademarks being recognized as a renowned trademark.

### ***Income taxes***

Income tax expense for the fiscal year ended September 30, 2011 was \$1.0 million, compared with an income tax expense of \$0.6 million (adjusted) in the fiscal year ended September 30, 2010. The change in income tax expense was mainly due to the increase of taxable income generated from PRC in fiscal year 2011 compared with fiscal year 2010.

### ***Loss from discontinued operations***

Champion Xinlixiang, which operated our Gaokao retake preparation and high-school supplementary tutoring business that we acquired in September 2009 from Mr. Junnan Ye and Mr. Xiujie Hu, incurred significant operating loss in the fiscal year ended September 30, 2011. As a result, we decided to discontinue such business and put the related assets and business up for sale.

In conjunction with the planned discontinuance of operations and to write down the related carrying amounts to their fair values less cost to sell, the goodwill, property, plant and equipment, and non-compete agreement relating to Champion Xinlixiang were impaired by \$0.8 million, \$1.0 million and \$0.3 million, respectively, for the fiscal year ended September 30, 2011, as compared to \$1.4 million, nil and \$0.3 million, respectively, for the fiscal year ended September 30, 2010.

The revenue and pre-tax loss from the discontinued operations included in our consolidated statement of operations were \$1.8 million and \$3.4 million, respectively, for the year ended September 30, 2011, as compared to \$2.2 million and \$2.2 million, respectively, for the year ended September 30, 2010.

### ***Net Loss***

As a result of the above factors, we incurred a net loss of \$3.8 million in the fiscal year ended September 30, 2011, compared to a net loss of \$1.9 million in the fiscal year ended September 30, 2010.

## **Fiscal Year Ended September 30, 2010 Compared to Fiscal Year Ended September 30, 2009**

### ***Net Revenues***

Our total net revenues increased by 8.2% (adjusted) to \$32.6 million(adjusted) in the fiscal year ended September 30, 2010 from \$30.1 million in the fiscal year ended September 30, 2009, as a result of growth in sales of our online education services, and books and reference materials.



*Online education services.* Net revenues from our online education services increased by 7.6% to \$24.0 million in the fiscal year ended September 30, 2010 from \$22.3 million in the fiscal year ended September 30, 2009. This increase was primarily due to overall growth in the total number of our online course enrollments to 1,211,000 in the fiscal year ended September 30, 2010 from over 1,071,000 in the fiscal year ended September 30, 2009. Our accounting courses continued to account for the majority of our course enrollments with a total enrollment of 970,000 in the fiscal year ended September 30, 2010 while enrollments in our self-taught study process monitoring programs for self-taught learners and our healthcare and construction engineering courses, also increased. Of this revenue increase, approximately \$1.2 million, \$3.0 million, \$3.2 million, and \$6.4 million were generated from our construction engineering courses, accounting continuing education courses, healthcare courses, and regular and premium classes for Accounting Professional Qualification Examination, respectively. Our revenue growth rate in the fiscal year ended September 30, 2010 was partially impacted by the business adjustment of our information technology courses in the fourth quarter ended September 30, 2010. After conducting a cost benefit analysis, we ceased to provide online training courses for information technology contests. In addition, we also experienced overall decrease in enrollments and revenues of our CPA Qualification Examination courses from 131,000 and \$5.6 million, respectively, in the fiscal year ended September 30, 2009 to 120,000 and \$4.4 million, respectively, in the fiscal year ended September 30, 2010.

*Books and reference materials.* Net revenues from our sales of books and reference materials increased by 45.4% to \$3.9 million in the fiscal year ended September 30, 2010 from \$2.7 million in the fiscal year ended September 30, 2009. The increase in our books and reference materials revenues was due primarily to an overall increase in cash payments received. We sell books and reference materials through distributors and grant some major distributors extended credit terms. Due to the extended credit terms, revenue recognition for such sales is deferred until cash is collected from such major distributors.

*Others.* Our other net revenues decreased to \$4.7 million (adjusted) in the fiscal year ended September 30, 2010 from \$5.1 million in the fiscal year ended September 30, 2009, primarily due to minimal revenue recorded from our business start-up training courses as we temporarily cut back the business in early fiscal year 2010 for business and management team adjustment and gradually resumed delivering the training courses after April 2010. The decrease was partially offset by revenues generated from our offline information technology courses and related services, and course production services. Other revenues also included sales of our platform production services, magazine content production services, tax and accounting related services through our [www.chinaacc.com](http://www.chinaacc.com) website, in-person professional training for accounting firms, and, to a lesser extent, other value-added services offered through our websites.

### **Gross Profit**

Our gross profit increased by 9.6% (adjusted) to \$17.2 million (adjusted) in the fiscal year ended September 30, 2010 from \$15.7 million in the fiscal year ended September 30, 2009. Our gross margin increased slightly to 52.9% (adjusted) in the fiscal year ended September 30, 2010 from 52.2% in the fiscal year ended September 30, 2009.

### **Operating Expenses**

Our operating expenses increased by 26.3% (adjusted) to \$17.9 million (adjusted) in the fiscal year ended September 30, 2010 from \$14.2 million in the fiscal year ended September 30, 2009, primarily as a result of additional share-based compensation expenses arising from our share options granted in the first quarter of the fiscal year ended September 30, 2010; impairment of purchased call option acquired with the acquisition of Zhengbao Yucai; significant bad debts provision; increase in commissions paid to agents; increased salary and welfare expenses for business expansion; and additional professional expenses associated with being a U.S. public company. Such increase was partially offset by the significant decrease in advertising and promotional activities as we exercised tight control of our overall expenses.

*Selling expenses.* Our selling expenses increased by 6.8% (adjusted) to \$7.2 million (adjusted) in the fiscal year ended September 30, 2010 from \$6.7 million in the fiscal year ended September 30, 2009. This increase resulted primarily from higher salaries and welfare expenses in customer service, and sales and marketing services as we maintained the number of staff at a high level to provide better service to our course participants and other customers, and to promote our business; increase in commissions paid to agents due to an increase in the sales of our courses. Such increase was partially offset by the significant decrease in advertising and promotional activities as we exercised tight control of our overall expenses.

*General and administrative expenses.* Our general and administrative expenses increased by 41.8% (adjusted) to \$10.5 million (adjusted) in the fiscal year ended September 30, 2010 from \$7.4 million in the fiscal year ended September 30, 2009. This increase was primarily due to \$2.0 million share-based compensation expenses we incurred in the fiscal year ended September 30, 2010; after an assessment of specific evidence indicating doubtful collection, \$2.2 million bad debts provision was made for certain accounts receivables that have been outstanding for more than 360 days with respect to the business start-up training business, accounting continuing education courses and ITAT contest; increased headcount for business expansion, and additional professional expenses associated with being a U.S. public company. Our administrative staff salaries and related expenses increased to \$2.6 million (adjusted). Our professional fees increased to \$1.4 million. Most of our other components of general and administrative expenses also increased due to the expansion of our business.

*Impairment of goodwill, intangible assets and purchased call options.* Zhengbao Yucai, which operates the business of start-up training services we acquired in March 2009, incurred net losses for the fiscal years of 2009 and 2010. In addition, in late 2009, we noted that Mr. Liang Ma, Yinglun Yucai, a company owned by Mr. Liang Ma, and Global Education Consortium Group Co., Limited, a company owned by Mr. Liang Ma's wife engaged in competing businesses which is prohibited under the purchase agreement. As a result, we filed an arbitration application in January 2010 with the China International Economic and Trade Arbitration Commission against Mr. Liang Ma and the other related parties. For more information about the arbitration, please see "Item 8. Financial Information-Legal Proceedings." Under these circumstances, we performed impairment tests for the goodwill, other intangible assets and the purchased call options acquired with the acquisition of the start-up training business as of September 30, 2010. Based on the impairment tests, there was no impairment of goodwill and other intangible assets as the business start-up training business is expected to be profitable in the future. However, the option to acquire 49% equity interest of a company owned by Yinglun Yucai was fully impaired by \$0.03 million and the option to acquire 30% equity interest in Zhengbao Yucai was impaired by \$0.13 million. The option to acquire additional equity interest in Zhengbao Yucai was not fully impaired as of September 30, 2010 because it was possible at that time that we would exercise the option considering the prospect of the business start-up training business.

#### ***Other Operating Income***

In the fiscal year ended September 30, 2010, we had other operating income of \$0.07 million which was a one-time subsidy we received from the Beijing Haidian District Bureau of Finance for one of our trademarks being recognized as a renowned trademark. In the fiscal year ended September 30, 2009, we had other operating income of \$0.3 million, which was a one-time subsidy of listing expenses we received from the Management Committee of Zhongguancun Technology Park.

#### ***Income taxes***

Income tax expense for the fiscal year ended September 30, 2010 was \$0.6 million (adjusted), compared with an income tax expense of \$1.5 million in the fiscal year ended September 30, 2009.

#### ***Loss from discontinued operations***

Champion Xinlixiang, which operates the Gaokao retake preparation and high-school supplementary tutoring business that we acquired in September 2009 from Mr. Junnan Ye and Mr. Xiujie Hu, incurred significant operating loss in the fiscal year ended September 30, 2011. As a result, we decided to discontinue such business and put the related assets and business up for sale.

Based on the impairment tests performed as of September 30, 2010, the related goodwill, non-compete agreement and option to purchase the remaining 40% equity interest in Champion Xinlixiang were impaired by \$1.4 million, \$0.3 million, and \$0.5 million, respectively, for the fiscal year ended September 30, 2010. The revenue and pre-tax loss from the discontinued operations included in our consolidated statement of operations were \$2.2 million and \$2.2 million, respectively, for the year ended September 30, 2010.

#### ***Net Loss***

As a result of the above factors, we incurred a net loss of \$1.9 million in the fiscal year ended September 30, 2010, compared to a net income of \$1.2 million in the fiscal year ended September 30, 2009.

### **B. Liquidity and Capital Resources**

Historically, we have financed our operations primarily through internally generated cash and bank loans. As of September 30, 2009, 2010 and 2011, we had approximately \$55.1 million (adjusted), \$60.2 million (adjusted) and \$60.3 million in cash and cash equivalents, including bank term deposits and restricted cash, respectively. As of September 30, 2011, our cash and cash equivalents of \$49.7 million primarily consisted of cash on hand, bank deposits, and AAA rated money market funds which are unrestricted as to withdrawal and use and are deposited with banks in China and Hong Kong. We intend to finance our future working capital requirements and capital expenditures from net cash generated from operating activities and existing cash and cash equivalents. In the opinion of the Company, our working capital is sufficient for our present requirements.

On November 20, 2008, we announced the adoption by our board of directors of a share repurchase program. The program authorized us to repurchase up to \$10 million worth of our issued and outstanding ADSs from time to time in open market transactions on the NYSE (or NYSE Arca, prior to February 4, 2009). We implemented this share repurchase program over the 12 months starting from November 20, 2008, in a manner consistent with market conditions and the interest of our shareholders. Our board decided to extend the share repurchase program for 12 months in November 2009 and November 2010, respectively, and it was scheduled to end on November 19, 2011. During the extension period from November 20, 2010 to November 19, 2011, we were authorized to repurchase up to \$3.8 million of our issued and outstanding ADSs, with such \$3.8 million representing the unused portion of the \$10 million previously approved by the board. On April 29, 2011, the board of directors approved an increase of the repurchase quota under the share repurchase program. The expanded share repurchase program authorizes the repurchase of up to an additional \$10 million of our ADSs (which makes the total repurchase quota under the share repurchase program \$20 million ADSs) and would be valid until April 28, 2012. On February 28, 2012, the board of directors decided to further extend the share repurchase program for 12 months until April 28, 2013. The repurchases will be made at prevailing market prices, in negotiated transactions off the market, in block trades, pursuant to Rule 10b-18 of the Exchange Act and a 10b5-1 plan (the 10b5-1 plan allows us to repurchase our ADSs during periods in which we may be in possession of material non-public information) or otherwise. The purchases will be made subject to restrictions relating to volume, price and timing. The timing and extent of any purchases will depend upon market conditions, the trading price of our ADSs and other factors. Our board of directors will review the share repurchase program periodically, and may authorize adjustment of its terms and size accordingly. As of December 31, 2011, we had repurchased an aggregate of 3,603,017 ADSs, representing 14,412,068 ordinary shares, on the open market for a total cash consideration of \$14.2 million. We do not expect any share repurchases carried out under the share repurchase program to have a material impact on our liquidity or capital resources.

The following table summarizes our cash flows in the fiscal years ended September 30, 2009, 2010 and 2011:

	<b>For the Year Ended September 30,</b>		
	<b>2009</b>	<b>2010</b>	<b>2011</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>
	(In thousands)		
Net cash generated from operating activities	1,607	7,653	9,192
Net cash (used in) generated from investing activities	(41,534)	31,420	(9,843)
Net cash used in financing activities	(4,841)	(2,109)	(8,063)
Exchange rate effect on cash and cash equivalents	(18)	354	906
Net (decrease) increase in cash and cash equivalents	(44,786)	37,318	(7,808)
Cash and cash equivalents at beginning of the year	66,223	21,437	58,755
Cash and cash equivalents at end of the year*	<u>21,437</u>	<u>58,755</u>	<u>50,947</u>

\* Such balances include the cash and cash equivalents of Champion Xinlixiang, our discontinued operation.

CDEL Cayman, our ultimate holding company, may rely on dividends and other distributions on equity paid by our PRC subsidiaries for its cash requirements, but such dividends and other distributions are subject to restrictions under PRC law. See Note 16 to our consolidated financial statements included in this annual report.

### Operating activities

Net cash generated from operating activities was \$9.2 million in the fiscal year ended September 30, 2011, and compared to \$7.7 million and \$1.6 million in the fiscal years ended September 30, 2010 and 2009, respectively.

Net cash generated from operating activities in the fiscal year ended September 30, 2011 was primarily attributable to (i) net income before non-cash items including share based compensation expenses, depreciation and amortization, and allowance for doubtful accounts, and impairment on goodwill, property, plant and equipment, intangible assets and purchased call options, (ii) increase in accrued expenses and other liabilities of \$1.1 million, (iii) increase in income tax payable of \$0.6 million, and (v) increase in refundable fees of \$0.9 million. The increase in operating cash flow was partially offset by increase in prepayments and other assets of \$1.1 million and decrease in deferred tax assets and liabilities of \$1.1 million.

Net cash generated from operating activities in the fiscal year ended September 30, 2010 was primarily attributable to (i) net income before non-cash items including share based compensation expenses, depreciation and amortization, allowance for doubtful accounts, and impairment on goodwill, intangible assets and purchased call options, (ii) increase in accrued expenses and other liabilities of \$1.9 million, and (iii) increase in deferred revenue of \$1.0 million. The increase in operating cash flow was partially offset by increase in accounts receivable of \$2.0 million.

Net cash generated from operating activities in the fiscal year ended September 30, 2009 was primarily attributable to (i) our net income before non-cash items, (ii) an increase in accrued expenses and other liabilities of \$0.8 million, and (iii) an increase in our deferred revenue of \$2.1 million. The increase in operating cash flow was partially offset by an increase in accounts receivable, deferred costs, and decrease in refundable fees of \$4.3 million, \$0.8 million, and \$2.9 million, respectively.

### **Investing activities**

Net cash used in investing activities was \$9.8 million in the fiscal year ended September 30, 2011, compared to net cash generated from investing activities of \$31.4 million in the fiscal year ended September 30, 2010 and net cash used in investing activities of \$41.5 million in the fiscal years ended September 30, 2009, respectively.

Net cash used in investing activities in the fiscal year ended September 30, 2011 was primarily attributable to (i) the purchase of property, plant and equipment in the amount of \$2.0 million, and (ii) purchase of term deposits of \$7.6 million. The decrease in cash flow was partially offset by the release of restricted cash of \$0.4 million.

Net cash generated from investing activities in the fiscal year ended September 30, 2010 was primarily attributable to (i) release of restricted cash of \$5.4 million, and (ii) decrease in term deposits of \$27.8 million. The increase in cash flow was partially offset by the purchase of property, plant and equipment in the amount of \$1.6 million.

Net cash used in investing activities in the fiscal year ended September 30, 2009 was primarily attributable to (i) our acquisition of the businesses of Zhengbao Yucai and Champion Xinlixiang with an aggregate amount of \$3.2 million, (ii) the purchase of property, plant and equipment, and other equipment in the amount of \$1.5 million, and (iii) an increase in restricted cash and term deposits of \$8.3 million and \$27.8 million, respectively.

### **Financing activities**

Net cash used in financing activities was \$8.1 million in the fiscal year ended September 30, 2011, compared to net cash used in financing activities of \$2.1 million and \$4.8 million in the fiscal years ended September 30, 2010 and 2009, respectively.

Net cash used in financing activities in the fiscal year ended September 30, 2011 was primarily attributable to the repurchase of our ADSs from the open market in the amount of \$8.1 million.

Net cash used in financing activities in the fiscal year ended September 30, 2010 was primarily attributable to the repurchase of our ADSs from the open market in the amount of \$2.2 million.

Net cash used in financing activities in the fiscal year ended September 30, 2009 was primarily attributable to (i) the repurchase of our ADSs from the open market in the amount of \$4.0 million, and (ii) payment of deferred initial public offering expenses of \$0.9 million.

### **Capital Expenditures**

We incurred capital expenditures of \$2.6 million, \$1.8 million, and \$5.5 million in the fiscal years ended September 30, 2011, 2010, and 2009, respectively. The amount of capital expenditures in the fiscal years ended September 30, 2011 and 2010 related primarily to our expenditures on property, plant and equipment, and software. The significant amount of capital expenditures in the fiscal year ended September 30, 2009 related primarily to our purchase of the business of Zhengbao Yucai and Champion Xinlixiang as well as expenditures on property, plant and equipment. From time to time, we may evaluate and make investments, acquisitions or divestments.

We believe that our current cash and cash equivalents, and anticipated cash flows from operations will be sufficient to meet our anticipated working capital requirements and capital expenditures for 12 months following the date of this annual report. Our online course platform can support significant growth in course enrollments and is easily adapted for the addition of new courses. We do, however, expect to spend money on the further development of our "Chinaacc" brand and other brands in the disciplines for which we offer courses. We do not expect our short-term and long-term cash requirements to be materially different.

Nevertheless, we may require additional sources of liquidity in the event of changes in business conditions or other future developments. Factors affecting our sources of liquidity include, for example, mergers and acquisitions, our sales performance, ability to control costs and expenses, and choice of financing arrangements. Any changes in the significant factors affecting our revenues from education services may cause material fluctuations in our cash generated from operations. See “Operating Results — Overview — Specific Factors Affecting Our Results of Operations” for a description of these significant factors. Changes in working capital, including any significant shortening or lengthening of our accounts receivable cycle or customer prepayment cycles, may also cause fluctuations in our cash generated from operations. If our sources of liquidity are insufficient to satisfy our cash requirements, we may seek to sell additional equity or debt securities to meet our cash needs. The sale of convertible debt securities or additional equity securities could result in dilution to our shareholders. The incurrence of indebtedness would result in debt service obligations and could result in operating and financial covenants that restrict our operations. We cannot assure you that future financing will be available in amounts or on terms acceptable to us, if at all.

Current PRC regulations permit our PRC subsidiaries to pay dividends to us only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. However, our PRC subsidiaries are required under PRC laws and regulations to allocate a portion of their annual after-tax profits, if any, to certain statutory reserves and funds prior to declaring and remitting dividends. For example, our PRC subsidiaries are required to allocate at least 10% of their after-tax profits to statutory reserves until such reserves reach 50% of their respective registered capital. Allocations to these statutory reserves and funds can be used only for specific purposes and are not transferable to us in the form of loans, advances or cash dividends. As a result, our PRC subsidiaries are restricted in their ability to transfer a portion of their net assets to us. Such limitations on the ability of our PRC subsidiaries to transfer funds to us could materially and adversely affect our ability to grow, make investments or acquisitions, pay dividends, and otherwise fund and conduct our businesses.

### **Inflation**

Inflation in China has not had a material impact on our results of operations to date. According to the National Bureau of Statistics of China, the change in China’s Consumer Price Index was -0.7%, 3.3% and 5.4% in the years 2009, 2010 and 2011, respectively. In January 2012, the change in China’s Consumer Price Index was 4.5%.

### **C. Research and Development**

Research and development does not constitute a material part of our business and we do not incur any material expenses related to research and development.

### **D. Trend Information**

Other than as disclosed elsewhere in this annual report, we are not aware of any trends, uncertainties, demands, commitments or events for the year ended September 30, 2011 that are reasonably likely to have a material adverse effect on our revenues, income, profitability, liquidity or capital resources, or that caused the disclosed financial information to be not necessarily indicative of future operating results or financial conditions.

### **E. Off-Balance Sheet Arrangements**

We do not currently have, and do not expect in the future to have, any outstanding off-balance sheet arrangements or commitments. In our ongoing business, we do not plan to enter into transactions involving, or otherwise form relationships with, unconsolidated entities or financial partnerships established for the purpose of facilitating off-balance sheet arrangements or commitments.

### **F. Tabular Disclosure of Contractual Obligations**

#### **Contractual Obligations and Commercial Commitments**

The following table sets forth our contractual obligations as of September 30, 2011:

	<b>Total</b>	<b>Payment Due by Period</b>				<b>Others</b>
		<b>Within 1 Year</b>	<b>1-3 Years</b>	<b>3-5 Years</b>	<b>More than 5 Years</b>	
Operating lease obligations (1)	5,250	2,941	2,309	—	—	—
Others (2)	170	—	—	—	—	170
<b>Total</b>	<b>5,420</b>	<b>2,941</b>	<b>2,309</b>	<b>—</b>	<b>—</b>	<b>170</b>

- (1) Our operating lease obligations primarily relate to our leased servers and bandwidth as well as our leased office spaces in China. The office leases expire at different times over the period from the date of this annual report through 2014, and will become subject to renewal. We will evaluate the need to renew each office lease on a case-by-case basis prior to its expiration.
- (2) Liabilities for unrecognized tax benefits. The balance disclosed under “Others” represents liabilities for which reasonable estimates about the timing of the payment cannot be made.

### Indebtedness

We currently have no indebtedness, and had no indebtedness as of September 30, 2011.

### G. Safe Harbor

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and as defined in the Private Securities Litigation Reform Act of 1995. See “Introduction—Forward-Looking Statements.”

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### A. Directors and Senior Management

The following table sets forth certain information relating to 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 18th Floor, Xueyuan International Tower, 1 Zhichun Road, Haidian District, Beijing 100083, the People’s Republic of China.

Name	Age	Position
Zhengdong Zhu	43	Chairman of the Board of Directors, Chief Executive Officer
Baohong Yin	44	Deputy Chairman of the Board of Directors
Hongfeng Sun	45	Vice President, Director
Xiaoshu Chen	46	Independent Director
Annabelle Yu Long	39	Director
Liankui Hu	61	Independent Director
Carol Yu	49	Independent Director
Ping Wei	40	Chief Financial Officer

*Zhengdong Zhu* is co-founder, chairman of the board and chief executive officer of our company and is responsible for the overall management operations and strategic direction of our company. Prior to co-founding our company in 1998, Mr. Zhu worked at the Beijing Huake Hi-Tech Co., Ltd., a communications products and computer facilities company, as an engineer, manager of network department and vice general manager in charge of marketing and sales from 1995 to 1998. From 1989 to 1995, Mr. Zhu worked as an engineer in the area of electronic communications technology at the research department of North China Institute of Electro-Optics Technology. Mr. Zhu graduated from the Radio Engineering Department of the Southeast University in China with a bachelor’s degree in radio engineering in 1989, and obtained a graduate certificate from the management science department in Sichuan University in China in 2001. Mr. Zhu and Baohong Yin, our director and deputy chairman, are husband and wife.

*Baohong Yin* is co-founder, director and deputy chairman of our company. From 1989 to 2004, Ms. Yin worked as engineer, vice director of laboratory, senior engineer, director of laboratory and vice-general engineer at Beijing Uni-Construction Dadi Concrete Building Components Co., Ltd (previously known as Beijing Residential Construction Component Manufacturer). Ms. Yin graduated in 1989 from the Civil Engineering Department of Southeast University in China with a bachelor’s degree in civil engineering. She was also conferred the qualification as a senior engineer by the Beijing Advanced Specialized Technology Committee in 1999. Baohong Yin and Zhengdong Zhu, our chairman and chief executive officer, are wife and husband.

*Hongfeng Sun* is co-founder, director and vice president of our company. Prior to co-founding our company, he worked at Sichuan Champion Hi-Tech Co., Ltd., a company in Sichuan, China engaging in system integration. From 1991 to 1998, Mr. Sun worked as an assistant general manager in charge of market development at Nanjing Bada Computer System Co., Ltd. From 1989 to 1991, Mr. Sun worked at Port Authority of Nanjing as a system engineer. Hongfeng Sun graduated in 1989 from the Radio Engineering Department of Southeast University in China with a bachelor’s degree in radio engineering.

*Xiaoshu Chen* is an independent director of our company, and currently a professor and an assistant director at the Department of Radio Engineering of SISE Southeast University in China. From 1985 to 2001, Professor Chen worked as an assistant lecturer, lecturer and assistant professor at the same department. Professor Chen has almost 20 years of experience in communication systems and network research. He graduated in 1985 from the Department of Radio Engineering of the Nanjing Institute of Technology in China with a bachelor's degree in engineering. He obtained his master's degree in engineering in 1990 from the same university.

*Annabelle Yu Long* became a director of our company on November 18, 2008. She has served as Chief Executive of Bertelsmann China Corporate Center and Managing Director of Bertelsmann Asia Investments, or BAI, the strategic investment arm of Bertelsmann AG since 2008. BAI is an affiliate of Bertelsmann Asia Investments AG, a shareholder of the company. In addition, she has served as board member for BMG Right Management Germany GMBH. From 2005 to 2007, Ms. Long was a principal of Bertelsmann Digital Media Investments. Ms. Long received her bachelor's degree in science and electric engineering from the University of Electronic Science and Technology in China in 1994, and her master's degree in business administration from Stanford Graduate School of Business in 2005.

*Liankui Hu* is an independent director of our company. He has also served as chairman on the boards of directors of the following technology companies since 1998, Beijing Teamsun Technology Co., Ltd., and Beijing Huasun Mingtian Technology Co. Ltd. From 1987 to 1998, Mr. Hu had worked for the Sixth Electronics Institute of the Ministry of Information Industry as deputy president, for Beijing Shenyan System Co., Ltd. as general manager, and for Beijing Huasun Computer Co., Ltd. as general manager. He was a lecturer in School of Economics and Management, Tsinghua University in China from 1985 to 1987. Mr. Hu received his bachelor's degree in engineering from Radio Engineering Department of Tsinghua University in 1982, and his master's degree from School of Economics and Management of Tsinghua University in 1985.

*Carol Yu* is an independent director of our company. Since 2004, Ms. Yu has been serving as co-president and chief financial officer of Sohu.com Inc., an Internet portal company listed on the Nasdaq Global Market. From 2000 to 2001, Ms. Yu served as vice president of Guangdong Kelon Refrigerating Company Limited, a home appliance manufacturer in China. From 1995 to 2000, Ms. Yu served as senior vice-president at the investment banking department of Donaldson Lufkin & Jenrette Securities Corporation in Hong Kong. Prior to that, Ms. Yu also worked with Arthur Andersen Hong Kong and Beijing for ten years and was a partner of the audit division, and held the position of general manager at Arthur Andersen-Hua Qiang, the joint venture accounting firm formed between Arthur Andersen and the Ministry of Finance in China. Ms. Yu obtained her bachelor's degree in accounting from The Hong Kong Polytechnic University. Ms. Yu is a Hong Kong Certified Public Accountant.

*Ping Wei* is our chief financial officer. Ms. Wei has extensive international finance, accounting and audit experience. From 2005 to 2008, Ms. Wei worked with New Oriental Education and Technology Group (NYSE: EDU) as its director of finance and controller. In 2004, Ms. Wei was the head for EDU's North American operation. Prior to that, Ms. Wei worked with Lorus Therapeutics Inc., or Lorus, a Canadian biopharmaceutical company listed on both the Toronto Stock Exchange and the American Stock Exchange as its acting chief financial officer and controller and previously as its assistant controller. Prior to working at Lorus, Ms. Wei worked as an auditor for seven years with Deloitte & Touche in Toronto and Arthur Andersen in Beijing. Ms. Wei is a Canadian Chartered Accountant and a US CPA with the State of Illinois. Ms. Wei received her bachelor's degree in international accounting from the Central University of Finance and Banking in Beijing in 1993.

## **B. Compensation**

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

For the fiscal year ended September 30, 2011, we and our subsidiaries paid aggregate cash compensation of approximately \$0.5 million to our directors and executive officers as a group. We do not pay or set aside any amounts pursuant to a bonus plan or for pension, retirement or other benefits for our officers and directors.

### **Share Options, Restricted Shares and Share Incentive Plans**

We adopted our Share Incentive Plan, or the Prior Plan, on April 18, 2008. We adopted on July 2, 2008, and amended and restated on February 16, 2009, our 2008 Performance Incentive Plan, or the New Plan. Our incentive plans are intended to promote our success and to increase shareholder value by providing an additional means to attract, motivate, retain and reward selected directors, officers, employees, lecturers and other eligible persons. An aggregate of 11,652,556 ordinary shares are reserved for issuance under the Prior Plan. Subject to any amendment of the New Plan, the maximum number of ordinary shares that may be issued pursuant to the New Plan is 11,267,992 ordinary shares as of September 30, 2011, plus an automatic annual increase on October 1 of each calendar year, by an amount equal to the lesser of (i) 1% of the total number of ordinary shares issued and outstanding on September 30 of the same calendar year, (ii) 1,418,977 ordinary shares, or (iii) such number of ordinary shares as may be determined by our board of directors.

Most options issued under our share incentive plans generally vest over a period of four years, with 25% vesting on the first anniversary of the vesting start date designated in the board resolution granting such options and the remaining 75% vesting in six substantially equal semi-annual installments. The first installment vests on the last day of the sixth month following the month in which the first anniversary of the vesting start date occurs and an additional installment vests on the last day of every six months thereafter.

On September 27, 2011, we granted 1,000,600 and 400,000 options to employees and five non-executive directors, respectively, at an exercise price of \$0.615 per share, which equaled the per share value of our ADS on the NYSE at the close of trading on September 27, 2011. The vesting term of the 1,000,600 options granted to employees is a two-year period, with four equal semi-annual installments, while the 400,000 options granted to five non-executive directors had been fully vested on the same day. In addition, we reduced the exercise price of 8,066,700 and 1,398,300 outstanding share options under the Prior Plan from \$0.82 per share to \$0.615, which equaled the closing price of our ADSs on NYSE at the close of trading on September 27, 2011, and zero per share, respectively. Furthermore, the re-priced options had been accelerated to be fully vested on the same day.

On December 3, 2010, we issued each of our five non-executive directors 20,000 restricted shares of which restrictions will be removed on the first anniversary of the issue date.

On September 27, 2011, we determined to provide three-years interest free, full recourse loans to employees and lecturers to exercise their options. As of December 31, 2011, 6,370,868 options had been exercised using this facility, amounting to a total loan amount of \$3.9 million.

Under the Prior Plan, we have to date granted options for the purchase of a total of 11,045,500 ordinary shares to selected officers, employees, and lecturers. Pursuant to the New Plan, we have to date granted options for the purchase of a total of 800,000 ordinary shares and issued 157,143 restricted shares to five non-executive directors and granted options to purchase 2,362,500 ordinary shares to other selected employees. As of February 24, 2012, there were outstanding options to purchase 4,226,652 ordinary shares, out of which options to purchase approximately 3 million ordinary shares have vested under their current terms. We expect to recognize significant share-based compensation expenses for the remaining vesting period of the outstanding options, which may materially impact our future results of operations. During the fiscal years of September 30, 2009, 2010 and 2011, we recognized share-based compensation expenses of \$3.9 million, \$4.4 million and \$6.0 million, respectively.

Options granted under our share incentive plans generally do not vest unless the grantee remains under our employment or in service with us on the given vesting date. Generally, if the grantee's employment or service with us is terminated for cause, all such grantee's options under our share incentive plans, vested and unvested, immediately terminate and become unexercisable. On the other hand, if the grantee's employment or service with us is terminated for any reason other than for cause, all such grantee's vested options terminate and become unexercisable ninety days following the grantee's last day of employment or service with us. In circumstances where there is a death or disability of the grantee, generally all unvested options immediately terminate and become unexercisable while vested options terminate and become unexercisable twelve months after the last date of employment or service with us. Generally, all unvested options granted under the Plan become fully vested immediately upon a change in the control of our company.

Our board of directors may amend, alter, suspend, or terminate our share incentive plans at any time, provided, however, that our board of directors must first seek the approval of the participants of our share incentive plans if such amendment, alteration, suspension or termination would adversely affect the rights of participants under any option granted prior to that date. Without further action by our board of directors, both Prior Plan and the New Plan will terminate in 2018.



The table below sets forth the option grants and restricted share issuance made to our directors and executive officers pursuant to our share incentive plans:

<u>Name of Recipient</u>	<u>Type of Incentive Securities</u>	<u>Number of Ordinary Shares Issued or to be Issued</u>	<u>Exercise Price per Ordinary Share</u>	<u>Date of Grant or Issue</u>	<u>Vesting Start Date</u>	<u>Date of Expiration</u>
Carol Yu	restricted ordinary shares	20,000 ordinary shares	not applicable	December 3, 2010	restriction removed on the first anniversary of the issue date	not applicable
	options to purchase ordinary shares	80,000	\$ 0.615	September 27, 2011	fully vested immediately on grant date	September 26, 2021
Baohong Yin	restricted ordinary shares	20,000 ordinary shares	not applicable	December 3, 2010	restriction removed on the first anniversary of the issue date	not applicable
	options to purchase ordinary shares	80,000	\$ 0.615	September 27, 2011	fully vested immediately on grant date	September 26, 2021
Xiaoshu Chen	restricted ordinary shares	20,000 ordinary shares	not applicable	December 3, 2010	restriction removed on the first anniversary of the issue date	not applicable
	options to purchase ordinary shares	80,000	\$ 0.615	September 27, 2011	fully vested immediately on grant date	September 26, 2021
Annabelle Yu Long	restricted ordinary shares	20,000 ordinary shares	not applicable	December 3, 2010	restriction removed on the first anniversary of the issue date	not applicable
	options to purchase ordinary shares	80,000	\$ 0.615	September 27, 2011	fully vested immediately on grant date	September 26, 2021
Liankui Hu	restricted ordinary shares	20,000 ordinary shares	not applicable	December 3, 2010	restriction removed on the first anniversary of the issue date	not applicable
	options to purchase ordinary shares	80,000	\$ 0.615	September 27, 2011	fully vested immediately on grant date	September 26, 2021

### **C. Board Practices**

#### **Duties of Directors**

Under Cayman Islands law, our directors have a statutory duty of loyalty to act honestly in good faith with a view to our best interests. Our directors also have a duty to exercise the care, diligence and skills 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 second amended and restated memorandum of association and articles of association. A shareholder has the right to seek damages if a duty owed by our directors is breached.

The functions and powers of our board of directors include, among others:

- convening shareholders' meetings and reporting its work to shareholders at such meetings;
- implementing shareholders' resolutions;
- determining our business plans and investment proposals;
- formulating our profit distribution plans and loss recovery plans;
- determining our debt and finance policies and proposals for the increase or decrease in our registered capital and the issuance of debentures;
- formulating our major acquisition and disposition plans, and plans for merger, division or dissolution;
- proposing amendments to our second amended and restated memorandum of association and articles of association; and
- exercising any other powers conferred by the shareholders' meetings or under our second amended and restated memorandum of association and articles of association.

### **Terms of Directors and Executive Officers**

Each of our directors holds office until a successor has been duly elected and qualified unless the director was appointed by our board of directors, in which case such director holds office until the next annual meeting of shareholders at which time such director is eligible for reelection. All of our executive officers are appointed by and serve at the discretion of our board of directors.

### **Terms of Directors**

We currently have a board of seven directors divided into class A, class B and class C directors. Hongfeng Sun is the class A director. The class B directors are Baohong Yin, Annabelle Yu Long and Xiaoshu Chen. The class C directors are Zhengdong Zhu, Carol Yu and Liankui Hu. At our first annual general meeting after our initial public offering held in April 2009, Mr. Hongfeng Sun, retired as a class A director and was re-elected as the class A director. At the second annual general meeting after our initial public offering held in May 2010, all class B directors retired as class B directors and were re-elected as the Class B directors. At the third annual general meeting after our initial public offering held in May 2011, our Class C directors that are subject to retirement, i.e. Carol Yu and Liankui Hu, were re-elected as the Class C directors. At each subsequent annual general meeting after the third annual general meeting after our initial public offering, one third of the directors for the time being (or, if their number is not a multiple of three (3), the number nearest to but not greater than one third) will retire from office by rotation. A retiring director will be eligible for re-election. The directors to retire by rotation will include (so far as necessary to ascertain the number of directors to retire by rotation) any director who wishes to retire and not to offer himself for re-election. Any further directors so to retire will be those of the other directors subject to retirement by rotation who have been longest in office since their last re-election or appointment and so that as between persons who became or were last re-elected directors on the same day those to retire shall (unless they otherwise agree among themselves) be determined by lot. Our chief executive officer, which currently is Zhengdong Zhu, is not, while holding office, subject to retirement or be taken into account in determining the number of directors to retire in any year. There are no director service contracts with us or any of our subsidiaries and affiliated entities providing for benefits upon termination of employment.

### **Board Practices**

Our board of directors has established an audit committee, a compensation committee and a nomination committee.

#### ***Audit Committee***

Our audit committee consists of Carol Yu, Liankui Hu and Xiaoshu Chen. Carol Yu is the chairman of our audit committee. Our board of directors has determined that all of our audit committee members satisfy the "independence" requirements of relevant rules of the NYSE and Rule 10A-3 under the Securities Exchange Act of 1934. Carol Yu meets the criteria of an audit committee financial expert as set forth under the applicable rules of the SEC.

Our audit committee is responsible for, among other things:

- appointing the independent auditor;
- pre-approving all auditing and non-auditing services permitted to be performed by the independent auditor;
- setting clear hiring policies for employees and former employees of the independent auditor;
- reviewing with the independent auditor any audit problems or difficulties and management's responses;

- reviewing and approving all related party transactions on an ongoing basis;
- reviewing and discussing the annual audited financial statements with management and the independent auditor;
- reviewing and discussing with management and the independent auditor major issues regarding accounting principles and financial statement presentations;
- reviewing reports prepared by management relating to significant financial reporting issues and judgments;
- discussing earnings press releases with management, as well as financial information and earnings guidance provided to analysts and rating agencies;
- reviewing with management and the independent auditor the effect of regulatory and accounting initiatives, as well as off-balance sheet structures, on our financial statements;
- discussing policies with respect to risk assessment and risk management with management, internal auditors and the independent auditor;
- timely reviewing reports from management regarding all critical accounting policies and practices to be used by our company, all alternative treatments of financial information within U.S. GAAP that have been discussed with management and all other material written communications between the independent auditor and management;
- establishing procedures for the receipt, retention and treatment of complaints received from our employees regarding accounting, internal accounting controls or auditing matters, and the confidential, anonymous submission by our employees of concerns regarding questionable accounting or auditing matters;
- annually reviewing and reassessing the adequacy of our audit committee charter;
- such other matters that are specifically delegated to our audit committee by our board of directors from time to time;
- meeting separately, periodically, with management, internal auditors and the independent auditor; and
- reporting regularly to the full board of directors.

#### ***Compensation Committee***

Our compensation committee consists of Zhengdong Zhu, Carol Yu and Liankui Hu. Zhengdong Zhu is the chairman of our compensation committee. Under Section 303A.00 of the NYSE's Listed Company Manual, a foreign private issuer is permitted to follow "home country practice" in relation to the composition of its compensation committee. In this regard, we have elected to adopt the practices of our home country, the Cayman Islands, which does not require that any of the members of a company's compensation committee be independent directors. Our board of directors has determined that Carol Yu and Liankui Hu satisfy the "independence" requirements of relevant rules of the NYSE and Rule 10A-3 under the Securities Exchange Act of 1934, as amended, or the Exchange Act. Our chairman and chief executive officer, Zhengdong Zhu, does not meet the definition of independence under such applicable rules.

Our compensation committee is responsible for:

- reviewing and approving our overall compensation policies;
- reviewing and approving corporate goals and objectives relevant to the compensation of our chief executive officer, evaluating our chief executive officer's performance in light of those goals and objectives, reporting the results of such evaluation to the board of directors and determining our chief executive officer's compensation level based on this evaluation;
- determining the compensation level of our other executive officers;
- making recommendations to the board of directors with respect to our incentive-compensation plan and equity-based compensation plans;
- administering our equity-based compensation plans in accordance with the terms thereof; and
- such other matters that are specifically delegated to the compensation committee by our board of directors from time to time.

### ***Nomination Committee***

Our nomination committee consists of Zhengdong Zhu, Liankui Hu and Xiaoshu Chen. Zhengdong Zhu is the chairman of the nomination committee. Under the relevant NYSE rules, a foreign private issuer is permitted to follow “home country practice” in relation to the composition of its nomination committee. In this regard, we have elected to adopt the practices of our home country, the Cayman Islands, which does not require that any of the members of a company’s nomination committee be independent directors. Our board of directors has determined that Liankui Hu and Xiaoshu Chen satisfy the “independence” requirements of the relevant rules of the NYSE and Rule 10A-3 under the Exchange Act. Our chairman and chief executive officer, Zhengdong Zhu, does not meet the definition of independence under such applicable rules.

Our nomination committee is responsible for, among other things:

- seeking and evaluating qualified individuals to become new directors as needed;
- reviewing and making recommendations to the board of directors regarding the independence and suitability of each board member for continued service; and
- evaluating the nature, structure and composition of other board committees.

### **Corporate Governance**

Our board of directors has adopted a code of ethics, which is applicable to our senior executive and financial officers. In addition, our board of directors has adopted a code of conduct, which is applicable to all of our directors, officers, employees and advisors. We have made our code of ethics and our code of conduct publicly available on our website. In addition, our board of directors has adopted a set of corporate governance guidelines. The guidelines reflect certain guiding principles with respect to our board’s structure, procedures and committees. The guidelines are not intended to change or interpret any law, or our second amended and restated memorandum of association and articles of association.

### **Interested Transactions**

A director may vote with respect to any contract or transaction in which he or she is interested, provided that the nature of the interest of any director in such contract or transaction is disclosed by him or her at or prior to its consideration and any vote in that matter.

### **D. Employees**

We had 801, 803 and 847 full-time employees as of September 30, 2009, 2010 and 2011, respectively. In addition to the above full-time employees, we had approximately 113 part-time employees as of September 30, 2011, of whom 68 are tutors.

As required by PRC regulations, our full-time employees in the PRC participate in a government mandated employee benefits plan, pursuant to which certain pension benefits, medical care, employee housing fund and other welfare benefits are provided to our employees. PRC labor regulations require that our PRC subsidiaries and affiliated entities make contributions to the government for these benefits based on certain percentages of the employees’ salaries. We have no legal obligation for the benefits beyond the contributions made. The total amounts for such employee benefits, which were expensed as incurred, were approximately \$1.4 million, \$1.9 million and \$2.5 million for the years ended September 30, 2009, 2010 and 2011, respectively.

We recognize as expenses obligations for contributions to employee benefits plans for full-time employees in Hong Kong, including contributions payable under the Hong Kong Mandatory Provident Fund Schemes Ordinance. The total amount for our Hong Kong employee benefits was approximately \$2,000 for each of the years ended September 30, 2009, 2010 and 2011.

We believe that we maintain a good working relationship with our employees and we have not experienced any significant labor disputes. Our employees have not entered into any collective bargaining agreements.

We view staff training as essential for the development of our human resources and our growth. We aim to provide our staff at all levels with the skills and knowledge relevant to their jobs and their career development as well as to improve their work efficiency. We have both routine and developmental training programs for our staff. Routine training includes our orientation program for new employees and on-the-job training. Developmental training is geared towards staff promotion and providing updated or new course information.

Our staff training is mainly conducted in-house. From time to time, we also engage external trainers with the relevant expertise to train our staff in areas such as customer service and software development.

## E. Share Ownership

The following table sets forth information with respect to the beneficial ownership, within the meaning of Rule 13d-3 under the Exchange Act, of our ordinary shares as of February 24, 2012, the latest practicable date by:

- our directors and executive officers as a group;
- each person known to us to own beneficially more than 5% of our ordinary shares;

	Ordinary Shares Beneficially Owned	
	Number <sup>(1)</sup>	Percent <sup>(2)</sup>
<b>Directors and Executive Officers:</b>		
Zhengdong Zhu <sup>(3)</sup>	73,878,493	54.43%
Baohong Yin <sup>(4)</sup>	73,878,493	54.43%
Xiaoshu Chen <sup>(5)</sup>	3,079,800	2.27%
Hongfeng Sun <sup>(6)</sup>	1,719,840	1.27%
Ping Wei <sup>(7)</sup>	1,712,919	1.26%
Annabelle Yu Long	*	*
Liankui Hu	*	*
Carol Yu	*	*
Directors and Executive Officers Combined	80,931,055	59.70%
<b>Principal Shareholders:</b>		
Champion Education Holdings Limited <sup>(8)</sup>	46,396,800	34.22%
Champion Shine Trading Limited <sup>(9)</sup>	27,301,693	20.14%
Orchid Asia III, L.P., Orchid Asia Co-Investment Limited, Orchid China Master Fund Limited and YM Investment Limited <sup>(10)</sup>	19,513,053	14.39%
Artson Limited <sup>(11)</sup>	7,481,797	5.52%

\* Beneficially owns less than 1% of our outstanding ordinary shares.

- (1) The number of ordinary shares beneficially owned by each of the listed persons includes ordinary shares that such person has the right to acquire within 60 days after February 24, 2012.
- (2) Percentage of beneficial ownership for each of the persons listed above is determined by dividing (i) the number of ordinary shares beneficially owned by such person by (ii) the total number of ordinary shares outstanding, plus the number of ordinary shares such person has the right to acquire within 60 days after February 24, 2012. The total number of ordinary shares outstanding as of February 24, 2012 is 135,571,661.
- (3) Includes (i) 21,337,265 ordinary shares held by Champion Shine Trading Limited, (ii) 46,396,800 ordinary shares held by Champion Education Holdings Limited, (iii) 20,000 ordinary shares held by Baohong Yin, and (iv) 160,000 ordinary shares issuable upon exercise of options held by Baohong Yin. Champion Shine Trading Limited is a British Virgin Islands company whose sole shareholder is Zhengdong Zhu. Champion Education Holdings Limited is a British Virgin Islands company, with Zhengdong Zhu holding 80% of its equity interest and Baohong Yin holding 20% of its equity interest. Zhengdong Zhu and Baohong Yin are husband and wife. Therefore, Zhengdong Zhu may be deemed to share the voting and dispositive power over the ordinary shares held by Baohong Yin as well as the ordinary shares issuable upon exercise of options held by Baohong Yin. Zhengdong Zhu disclaims beneficial ownership of such 20,000 ordinary shares held by Baohong Yin and such 100,000 ordinary shares issuable upon exercise of currently exercisable options held by Baohong Yin, in each case except to the extent of his pecuniary interest. The business address of Zhengdong Zhu is 18th Floor, Xueyuan International Tower 1, Zhichun Road, Haidian District, Beijing 100083, China.
- (4) Includes (i) 21,337,265 ordinary shares held by Champion Shine Trading Limited; (ii) 46,396,800 ordinary shares held by Champion Education Holdings Limited, (iii) 20,000 ordinary shares held by Baohong Yin, and (iv) 160,000 ordinary shares issuable upon exercise of options held by Baohong Yin. Baohong Yin holds 20% of the equity interest in Champion Education Holdings Limited. Zhengdong Zhu holds 80% of the equity interest in Champion Education Holdings Limited and he is the sole shareholder of Champion Shine Trading Limited. Zhengdong Zhu and Baohong Yin are husband and wife. Baohong Yin may therefore be deemed to share the voting and dispositive power over ordinary shares held by Champion Shine Trading Limited, Champion Education Holdings Limited and Zhengdong Zhu. Baohong Yin disclaims beneficial ownership of the 21,337,265 ordinary shares held by Champion Shine Trading Limited and 46,396,800 ordinary shares held by Champion Education Holdings Limited, in each case except to the extent of her pecuniary interest. The business address of Baohong Yin is 18th Floor, Xueyuan International Tower, 1 Zhichun Road, Haidian District, Beijing 100083, China.
- (5) Includes (i) 2,899,800 ordinary shares held by Jetlong Investments Limited, (ii) 20,000 ordinary shares held by Xiaoshu Chen, and (iii) 160,000 ordinary shares issuable upon exercise of options held by Xiaoshu Chen. Jetlong Investments Limited is a British Virgin Islands company whose sole shareholder and sole director is Xiaoshu Chen. The business address of Xiaoshu Chen is Southeastern University, No. 2 Sipailou, Nanjing 210096, China.

- (6) Includes 1,719,840 ordinary shares held by Brilliant State Holdings Limited. Brilliant State Holdings Limited is a British Virgin Islands company whose sole shareholder and sole director is Hongfeng Sun. The business address of Hongfeng Sun is 18th Floor, Xueyuan International Tower, 1 Zhichun Road, Haidian District, Beijing 100083, China.
- (7) Includes 1,712,919 ordinary shares held by Easerich Group Limited, a British Virgin Islands company whose sole shareholder and sole director is Ping Wei. The address of Easerich Group Limited is P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands.
- (8) Includes 46,396,800 ordinary shares held by Champion Education Holdings Limited. Champion Education Holdings Limited is a British Virgin Islands company, with Zhengdong Zhu holding 80% of its equity interest and Baohong Yin holding 20% of its equity interest. Zhengdong Zhu and Baohong Yin are all the directors of Champion Education Holdings Limited. The address of Champion Education Holdings Limited is P.O. Box 957, Offshore Incorporations Centre, Road Town, Tortola, British Virgin Islands.
- (9) Includes 27,301,693 ordinary shares held by Champion Shine Trading Limited, a British Virgin Islands company whose sole shareholder and sole director is Zhengdong Zhu. The address of Champion Shine Trading Limited is Suites 1501-1503, 15th Floor, Gloucester Tower, The Landmark, 15 Queen's Road Central, Hong Kong.
- (10) Includes 13,494,910 ordinary shares held by Orchid Asia III, L.P., 417,439 ordinary shares held by Orchid Asia Co-Investment Limited, 880,628 ordinary shares as represented by 220,157 ADSs held by Orchid China Master Fund Limited, and 4,720,076 ordinary shares as represented by 1,180,019 ADSs held by YM Investment Limited. Orchid Asia III, L.P., Orchid Asia Co-Investment Limited and Orchid China Master Fund Limited are part of Orchid Asia Group, Limited, an investment complex that focuses on companies in Asia and China in particular. OAIH Holdings, L.P. is the general partner of Orchid Asia III, L.P. Orchid Asia Group Management Ltd. is the general partner of OAIH Holdings, L.P. which is in turn a wholly-owned subsidiary of Orchid Asia Group, Limited. YM Investment Limited is the controlling shareholder of Orchid Asia Group, Limited, and is wholly-owned by The Li 2007 Family Trust. The Li 2007 Family Trust is a revocable trust established under the laws of the British Virgin Islands with Ms. Lam Lai Ming, Veronica as the settlor, Managecorp Limited as trustee and Ms. Lam Lai Ming and her family members the beneficiaries. YM Investment Limited is also the controlling shareholder of Orchid Asia Co-Investment Limited. Orchid China Management (Cayman) Limited serves as the investment manager to Orchid China Master Fund Limited, which is in turn majority owned by YM Investment Limited. The address of Orchid Asia III, L.P., Orchid Asia Co-Investment Limited, Orchid China Master Fund Limited and YM Investment Limited is c/o Orchid Asia Hong Kong Management Co. Ltd., Suite 6110, 61/F, The Center, 99 Queen's Road, Central, Hong Kong.
- (11) Includes 7,481,797 ordinary shares held by Artson Limited, a British Virgin Islands company with a correspondence address at 22nd Floor, Hang Lung Centre, 2-20 Paterson Street, Causeway Bay, Hong Kong. Artson Limited is wholly-owned by Morningside Technology Investments Limited, a British Virgin Islands company, which is in turn ultimately wholly beneficially owned by a family trust established by Madam Chan Tan Ching Fen.

See “—B. Compensation” for more details on options and/or restricted shares granted to our directors and executive officers.

As of September 30, 2011, of the 127,800,673 issued and outstanding ordinary shares, approximately 28.6% of those ordinary shares are held in the U.S., all under one registered holder of record.

None of our existing shareholders has voting rights that differ from the voting rights of other shareholders. A change of control of our company may occur as a result of the transaction that occurred in October 2011 among Bertelsmann Asia Investment AG, CST and CEH. If CST and CEH subsequently default on their obligation under this transaction, BAI may own a significant portion of our company, resulting in a change of control of our company. See below “—E. Share Ownership — Historical Changes in Shareholdings of our Major Shareholders” for more details.

In April 2008, we adopted our Share Incentive Plan pursuant to which we have reserved 11,652,556 ordinary shares to be issued upon the exercise of share options that we may grant to certain employees and others. We adopted on July 2, 2008, and amended and restated on February 16, 2009, our 2008 Performance Incentive Plan pursuant to which the maximum number of ordinary shares that may be issued is 11,267,992 ordinary shares as of September 30, 2011, plus an automatic annual increase on October 1 of each calendar year, by an amount equal to the lesser of (i) 1% of the total number of ordinary shares issued and outstanding on September 30 of the same calendar year, (ii) 1,418,977 ordinary shares, or (iii) such number of ordinary shares as may be determined by our board of directors. For more information on options and/or restricted shares granted to our existing shareholders, see “Item 6.B. Director, Senior Management and Employees — Compensation — Share Options, Restricted Shares and Share Incentive Plans.”

### **Historical Changes in Shareholdings of our Major Shareholders**

In 2009, YM Investment Limited acquired an aggregate of 218,008 ordinary shares as represented by 54,502 ADSs from the open market. In 2010, Orchid China Master Fund Limited and YM Investment Limited acquired an aggregate of 3,111,180 ordinary shares as represented by 777,795 ADSs from the open market.

In 2010, Champion Shine Trading Limited acquired an aggregate of 175,804 ordinary shares as represented by 43,951 ADSs from the open market.

In May 2010, Champion International Holdings Limited transferred our ordinary shares then held by it to four BVI entities formed by its then shareholders including Champion Education Holdings Limited, a British Virgin Island company jointly owned by our co-founders and directors Zhengdong Zhu and Baohong Yin.

In October 2011, Bertelsmann Asia Investment AG (“BAI”) sold to CST 16,268,523 shares, of which 1,750,000 ordinary shares are represented by 437,500 ADSs, for US\$28,917,300. The purchase of the shares except the ADS was completed on December 8, 2011 and the purchase of the ADSs was completed on December 9, 2011. This purchase was funded by an interest-free promissory note (the “Note”) in the amount of US\$28,917,300 issued by CST and CEH to BAI on October 26, 2011. The Note matures on November 29, 2014. As collateral for the Note, CST and CEH have pledged 2,408,769 and 46,396,800 of their ordinary shares, respectively, or 48,805,569 in total, pursuant to the Deed of Share Charge by and among CST and CEH, on the one hand, and BAI, on the other, dated October 26, 2011.

## **ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS**

### **A. Major Shareholders**

Please refer to “Item 6.E. Directors, Senior Management and Employees — Share Ownership.”

### **B. Related Party Transactions.**

#### **Shareholders Agreement**

We have entered into a shareholders agreement with Orchid Asia III, L.P., Orchid Asia Co-Investment Limited and Artson Limited and our existing holders of ordinary shares. Pursuant to the shareholders agreement, we granted certain registration rights to holders of our registrable securities. Registrable securities include (i) our ordinary shares issuable or issued upon conversion of our preferred shares, (ii) any of our ordinary shares issued as a dividend or other distribution with respect to, in exchange for, or in replacement of, the shares referenced in (i), and (iii) any other ordinary shares owned or acquired by any of holders of our preferred shares, excluding, among others, shares sold in a public offering. On July 25, 2008, the parties amended the shareholders agreement solely for the purpose of revising the definition of a qualified public offering to be a firm commitment underwritten public offering of our ordinary shares as represented by ADSs on NYSE Arca.

Under the terms of the agreement, from the date that is six months after the closing of our initial public offering, which occurred on August 4, 2008, holders of a majority in interests of our then outstanding registrable securities may require us to effect the registration for the sale of their registrable securities. We are obliged to effect up to five demand registrations. We have the right to defer filing for a period of no more than 90 days if our board of directors in good faith determines that filing of such registration will be materially detrimental to us and our shareholders, but we can not utilize this right more than once in any twelve-month period.

Holders of registrable securities also have “piggyback” registration rights, pursuant to which they may require us to register all or any part of the registrable securities then held by such holders when we file any registration statements for purposes of effecting a public offering of our securities.

If any of the offerings relating to a demand registration or a piggyback registration involves an underwriting, the managing underwriter of any such offering has certain rights to limit the number of shares included in such registration. However, where the number of registrable securities included in an underwritten public offering is to be reduced, the securities other than registrable shares must be reduced before any registrable securities may be reduced, and the number of our registrable shares that are included in such offering may not be reduced to less than 75% of the aggregate number of our registrable shares requested to be included in such underwriting.

Holders of registrable securities may also require us to effect a registration on Form S-3 or Form F-3 and any related qualification or compliance, as applicable, for a public offering of all or a part of their registrable securities so long as we are entitled to use Form S-3 or Form F-3 for such offering. However, we are not obliged to effect any such registration, when (i) the aggregate price to the public of such offering is less than \$500,000, or (ii) within the six month period preceding the date of such request, we have already effected a registration other than the registration from which the registrable securities of such holders have been excluded. We have the right to defer such filing for a period of no more than 90 days if our board of directors in good faith determines that filing of such registration will be materially detrimental to us and our shareholders, but we can not utilize this right more than once during any twelve-month period.

We are generally required to pay all expenses relating to any demand, piggyback or F-3 or S-3 registration other than all selling expenses or other amounts payable to underwriters or brokers for selling shareholders, if applicable.

We will have no obligations to effect any demand, piggyback or F-3 or S-3 registration with respect to any registrable securities after five years following the consummation of our initial public offering.

#### **Agreements among CDEL Hong Kong, Champion Technology, Champion Education Technology, Beijing Champion and Its Shareholders**

See “Item 4.C. Information on the Company — Organizational Structure.”

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

Not applicable.

### **ITEM 8. FINANCIAL INFORMATION**

#### **A. Consolidated statements and other financial information.**

We have appended consolidated financial statements filed as part of this annual report. See “Item 18. Financial Statements.”

#### **Legal Proceedings**

We are not currently involved in any litigation, arbitration or administrative proceedings that could have a material adverse effect on our financial condition or results of operations. From time to time, we may be subject to various claims and legal actions arising in the ordinary course of business.

In late 2009, we noted that Mr. Liang Ma, Beijing Yinglun Yucai Education Consulting Co., Ltd. (or Yinglun Yucai), a company owned by Mr. Liang Ma and from which we acquired the business start-up training business, and Global Education Consortium Group Co., Limited, a company owned by Mr. Liang Ma’s wife, breached the purchase agreement with us and were engaged in competing businesses. As a result, we filed an arbitration application in January 2010 with the China International Economic and Trade Arbitration Commission, or CIETAC, against Mr. Liang Ma, Yinglun Yucai and Global Education Consortium Group Co., Limited, or the respondents. In June 2011, CIETAC ruled, among other things, that (1) Mr. Liang Ma shall surrender his 40% ownership interest in Zhengbao Yucai to us for no consideration; (2) the respondents shall cease operating their competing businesses; (3) the respondents shall pay us RMB3.8 million (\$0.6 million) in compensatory damages; and (4) the respondents shall cooperate with us in completing the handover procedures, which includes but is not limited to the transferring and/or handover to us certain trademark and original business contracts. CIETAC’s ruling on this matter is final.

#### **Dividend Policy**

On November 16, 2011, our Board of Directors approved and declared a special cash dividend of \$0.12 per ordinary share on its outstanding shares to shareholders of record as of the close of trading on December 15, 2011. Holders of ADS, each representing four ordinary shares of CDEL, were accordingly entitled to the cash dividend of \$0.48 per ADS.

We currently intend to retain most of our available funds and any future earnings to finance our business and to fund the growth and expansion of our business in the PRC, and, therefore, do not expect to pay any cash dividends on our ordinary shares, including those represented by ADSs, in the foreseeable future.



We are a holding company incorporated in the Cayman Islands. We may rely on dividends from our subsidiaries in China. Current PRC regulations permit our subsidiaries to pay dividends to us only out of their accumulated profits, if any, determined in accordance with PRC accounting standards and regulations. In addition, our subsidiaries in China are required to set aside each year a certain amount of their accumulated after-tax profits, if any, to fund certain statutory reserves. These reserves may not be distributed as cash dividends. Further, if our subsidiaries in China incur debt on their own behalf, the instruments governing the debt may restrict their ability to pay dividends or make other payments to us. In addition, under the New EIT Law, effective as of January 1, 2008, dividends from our PRC subsidiaries to us may be subject to a 10% withholding tax, subject to reduction by an applicable tax treaty with the PRC if they are derived from profits generated after January 1, 2008. For a detailed discussion, see “Item 3.D. Key Information — Risk Factors — Risks Relating to Our Corporate Structure and Restrictions on Our Industry — We may rely principally on dividends and other distributions on equity paid by our PRC subsidiaries for our cash requirements, but such dividends and other distributions are subject to restrictions under PRC law. Limitations on the ability of our PRC subsidiaries to transfer funds to us could materially and adversely affect our ability to grow, make investments or acquisitions, pay dividends, and otherwise fund and conduct our businesses,” and “Item 5.A. Operating and Financial Review and Prospects — Operating Results — Description of Key Line Items — Taxation — Enterprise Income Tax.” Any future determination to pay dividends, if any, will be made at the discretion of our board of directors and will be based upon our future operations and earnings, capital requirements and surplus, general financial condition, shareholders’ interests, contractual restrictions and other factors our board of directors may deem relevant.

Holders of our ADSs will be entitled to receive dividends, if any, subject to the terms of the deposit agreement, to the same extent as the holders of our ordinary shares. Cash dividends will be paid to the depository in U.S. dollars, which will distribute them to the holders of ADSs according to the terms of the deposit agreement. Other distributions, if any, will be paid by the depository to the holders of ADSs in any means it deems legal, fair and practical.

## B. Significant Changes

Except as disclosed elsewhere in this annual report, we have not experienced any significant changes since the date of our audited financial statements included in this report.

## ITEM 9. THE OFFER AND LISTING

### A. Offering and listing details.

#### Price Range of Our ADSs

Our ADSs were initially listed for trading on NYSE Arca under the symbol “DL.” On February 4, 2009, we transferred the listing and trading of our ADSs from NYSE Arca to the New York Stock Exchange, Inc., or the NYSE, under the same symbol “DL.” The following table sets forth the monthly high and low trading prices of our ADSs on the NYSE (or NYSE Arca, prior to February 4, 2009), for the periods indicated:

	<u>High</u>	<u>Low</u>
<b>Annual Highs and Lows</b>		
Fiscal Year 2008 (from July 30, 2008)	\$7.00	\$3.00
Fiscal Year 2009	\$8.90	\$2.08
Fiscal Year 2010	\$7.96	\$3.04
Fiscal Year 2011	\$5.48	\$1.85
<b>Quarterly Highs and Lows</b>		
First Fiscal Quarter of 2010	\$7.96	\$5.81
Second Fiscal Quarter of 2010	\$7.00	\$5.17
Third Fiscal Quarter of 2010	\$6.02	\$3.04
Fourth Fiscal Quarter of 2010	\$5.75	\$3.29
First Fiscal Quarter of 2011	\$5.48	\$3.80
Second Fiscal Quarter of 2011	\$5.14	\$3.74
Third Fiscal Quarter of 2011	\$4.06	\$1.85
Fourth Fiscal Quarter of 2011	\$3.57	\$2.05
<b>Monthly Highs and Lows</b>		
<b>2011</b>		
August	\$3.06	\$2.05
September	\$2.80	\$2.16
October	\$2.63	\$1.80
November	\$2.70	\$2.44
December	\$2.90	\$1.91
<b>2012</b>		
January	\$2.75	\$2.10
February (through February 23, 2012)	\$3.78	\$2.24

On February 23, 2012, the closing sale price of our ADSs as reported on the NYSE was \$3.50 per ADS.

**B. Plan of Distribution**

Not applicable.

**C. Markets**

See Item 9.A. above.

**D. Selling Shareholders**

Not applicable.

**E. Dilution**

Not applicable.

**F. Expenses of the Issue**

Not applicable.

**ITEM 10. ADDITIONAL INFORMATION**

**A. Share capital**

Not applicable.

**B. Memorandum of Association and Articles of Association**

We incorporate by reference into this annual report the description of our second amended and restated memorandum of association and articles of association contained in “Description of Share Capital” of our F-1 registration statement (File No. 333-152167) originally filed with the Securities and Exchange Commission on July 7, 2008, as amended.

**Differences in Corporate Law**

China Distance Education Holdings Limited was incorporated as an exempted company with limited liability in the Cayman Islands in January 2008 under the Companies Law of the Cayman Islands, or the Company Law. Our corporate affairs are governed by our second amended and restated memorandum of association and articles of association, the Cayman Islands Companies Law and the common law of the Cayman Islands.

The Companies Law is modeled after similar laws in the United Kingdom but does not follow recent changes in United Kingdom laws. In addition, the Companies Law differs from laws applicable to United States corporations and their shareholders. Set forth below is a summary of the significant differences between the provisions of the Companies Law applicable to us and the laws applicable to companies incorporated in the United States.

*Mergers and Similar Arrangements.* A merger of two or more constituent companies under Cayman Islands law requires a plan of merger or consolidation to be approved by the directors of each constituent company and authorization by (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.

A merger between a Cayman parent company and its Cayman subsidiary or subsidiaries does not require authorization by a resolution of shareholders of that Cayman subsidiary if a copy of the plan of merger is given to every member of that Cayman subsidiary to be merged unless that member agrees otherwise. For this purpose a subsidiary is a company of which at least ninety percent (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.

Save in certain circumstances, a dissentient shareholder of a Cayman 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 save for the right to seek relief on the grounds that the merger or consolidation is void or unlawful.

In addition, there are statutory provisions that facilitate the reconstruction and amalgamation of companies, provided that the arrangement is approved by a majority in number of each class of shareholders and creditors (representing 75% by value) 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. The convening of the meetings and subsequently 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 majority 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 to promote interests adverse to those of the class;
- the arrangement is such that may be reasonably approved by an intelligent and honest man of that class acting in respect of his interest; 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 and accepted by holders of 90% of the shares within four months, 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 such 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 collusion.

If an arrangement and reconstruction is thus approved, the dissenting shareholder would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of Delaware corporations, providing rights to receive payment in cash for the judicially determined value of the shares.

*Shareholders' Suits.* In principle, we will normally be the proper plaintiff and a derivative action may not be brought by a minority shareholder. However, based on English authorities, which would in all likelihood be of persuasive authority in the Cayman Islands, exceptions to the foregoing principle apply in circumstances in which:

- a company is acting or proposing to act illegally or beyond the scope of its authority;
- the act complained of, although not beyond the scope of its authority, could be effected duly if authorized by more than a simple majority vote which has not been obtained; and
- those who control the company are perpetrating a "fraud on the minority."

*Corporate Governance.* Cayman Islands laws do not restrict transactions with directors, requiring only that directors exercise a duty of care and owe a fiduciary duty to the companies for which they serve. Under our second amended and restated memorandum of association and articles of association, subject to any separate requirement for audit committee approval under the applicable rules of the NYSE or unless disqualified by the chairman of the relevant board meeting, so long as a director discloses the nature of his interest in any contract or arrangement which he is interested in, such a director may vote in respect of any contract or proposed contract or arrangement in which such director is interested and may be counted in the quorum at such meeting.

### **C. Material Contracts**

We have not entered into any material contracts other than in the ordinary course of business and other than those described in "Item 4. Information on the Company" and in "Item 7. Major Shareholders and Related Party Transactions" or elsewhere in this annual report on Form 20-F.

### **D. Exchange Controls**

#### **Regulation of Foreign Exchange**

The PRC government imposes restrictions on the convertibility of the Renminbi and on the collection and use of foreign currency by PRC entities. Under current regulations, the Renminbi is convertible for current account transactions, which include dividend distributions, interest payments, and the import and export of goods and services. Conversion of Renminbi into foreign currency and foreign currency into Renminbi for capital account transactions, such as direct investment, portfolio investment and loans, however, is still generally subject to the prior approval of SAFE.

Under current PRC regulations, foreign-invested enterprises such as our PRC subsidiaries are required to apply to SAFE for a Foreign Exchange Registration Certificate for Foreign-Invested Enterprise. With such a certificate (which is subject to review and renewal by SAFE on an annual basis), a foreign-invested enterprise may open foreign exchange bank accounts at banks authorized to conduct foreign exchange business by SAFE and may buy, sell and remit foreign exchange through such banks, subject to documentation and approval requirements. Foreign-invested enterprises are required to open and maintain separate foreign exchange accounts for capital account transactions and current account transactions. In addition, there are restrictions on the amount of foreign currency that foreign-invested enterprises may retain in such accounts.

### **Regulation of Foreign Exchange in Certain Onshore and Offshore Transactions**

In October 2005, SAFE issued the Notice on Issues Relating to the Administration of Foreign Exchange in Fund-Raising and Return Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Companies, or SAFE Circular 75, which became effective as of November 1, 2005. According to SAFE Circular 75, prior to establishing or assuming control of an offshore enterprise for the purpose of financing that offshore enterprise with assets or equity interests in an onshore enterprise in the PRC, each PRC resident, whether a natural or legal person, must complete certain overseas investment foreign exchange registration procedures with the relevant local SAFE branch. An amendment to the registration with the local SAFE branch is required to be filed by any PRC resident that directly or indirectly holds interests in that offshore enterprise upon either (i) the injection of equity interests or assets of an onshore enterprise to the offshore enterprise or (ii) any overseas fund-raising by such offshore enterprise after such injection. An amendment to the registration with the local SAFE branch is also required to be filed by such PRC resident when there is any material change involving a change in the capital of the offshore enterprise, such as (i) an increase or decrease in its capital, (ii) a transfer or swap of shares, (iii) a merger or division, (iv) a long-term equity or debt investment or (v) the creation of any security interests.

SAFE Circular 75 applies retroactively. As a result, PRC residents who established or acquired control of offshore companies that made onshore investments in the PRC in the past were required to complete the relevant overseas investment foreign exchange registration procedures by March 31, 2006. Under SAFE Circular 75, failure to comply with the registration procedures may result in restrictions on the relevant onshore entity, including restrictions on the payment of dividends and other distributions to its offshore parent or affiliate and restrictions on the capital inflow from the offshore entity, and may also subject relevant PRC residents to penalties under the PRC foreign exchange administration regulations.

As a Cayman Islands company, we are considered a foreign entity in China. If we purchase the assets or equity interests of a PRC company owned by PRC residents in exchange for our equity interests, such PRC residents will be subject to the registration procedures described in SAFE Circular 75. Moreover, PRC residents who are beneficial holders of our shares are required to register with SAFE in connection with their investment in us.

### **Dividend Distributions**

See “Item 8.A. Financial Information — Dividend Policy” in connection with our policy regarding dividend distributions. See also “Item 3.D. Key Information — Risk Factors — Risks Relating to Our ADS — You may not receive distributions on our ordinary shares or any value for them if such distribution is illegal or if any required government approval cannot be obtained in order to make such distribution available to you.”

### **E. Taxation**

*The following is a general summary of the material Cayman Islands, U.S. federal and People’s Republic of China income tax consequences relevant to an investment in our ADSs and ordinary shares. The discussion is not intended to be, nor should it be construed as, legal or tax advice to any particular prospective purchaser or current holders of our ADSs. The discussion is based on laws and relevant interpretations thereof in effect as of the date of this annual report, all of which are subject to change or different interpretations, possibly with retroactive effect. The discussion does not address United States state or local tax laws, or tax laws of jurisdictions other than the Cayman Islands, the People’s Republic of China and the United States.*

#### **Cayman Islands Taxation**

The Cayman Islands currently levies no taxes on individuals or corporations based upon profits, income, gains or appreciations and there is no taxation in the nature of inheritance tax or estate duty or withholding tax applicable to us or to any holder of ADSs or ordinary shares. 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 after execution brought within the jurisdiction of the Cayman Islands. No stamp duty is payable in the Cayman Islands on transfers of shares of Cayman Islands companies except those which hold interests in land in 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.

Pursuant to Section 6 of the Tax Concessions Law (1999 Revision) of the Cayman Islands, we have obtained an undertaking from the Governor-in-Cabinet:

- that no law which is enacted in the Cayman Islands imposing any tax to be levied on profits or income or gains or appreciations shall apply to CDEL Cayman or its operations; and
- that the aforesaid tax or any tax in the nature of estate duty or inheritance tax shall not be payable on the shares, debentures or other obligations of CDEL Cayman.

The undertaking for CDEL Cayman is for a period of twenty years from January 29, 2008.

### **People's Republic of China Taxation**

In 2007 China passed a new Enterprise Income Tax Law, or the New EIT Law, and its implementing rules, both of which became effective on January 1, 2008. The New EIT Law created a new "resident enterprise" classification, which, if applied to us, would impose a 10% withholding tax on dividends payable to our non-PRC enterprise shareholders and with respect to gains derived by our non-PRC enterprise shareholders from disposition of our shares or ADSs. The New EIT Law and its implementing rules are unclear as to how to determine a PRC "resident enterprise" status for non-Chinese enterprise or group enterprise controlled entities. See "Item 3.D. Key Information — Risk Factors — Under China's New EIT Law, we may be classified as a 'resident enterprise' of China. Such classification could result in unfavorable tax consequences to us and our non-PRC shareholders."

If we are not deemed as a resident enterprise, then dividends payable to our non-PRC shareholders and gains from disposition of our shares of ADSs by our non-PRC shareholders will not be subject to PRC income tax withholding.

### **United States Federal Income Taxation**

This discussion describes the material U.S. federal income tax consequences to U.S. Holders (as defined below) of the purchase, ownership and disposition of our ADSs or ordinary shares. This discussion does not address any aspect of U.S. federal gift or estate tax, or the state, local or non-U.S. tax consequences of an investment in our ADSs and ordinary shares. This discussion applies to you only if you beneficially own our ADSs or ordinary shares as capital assets for tax purposes. This discussion does not apply to you if you are a member of a class of holders subject to special rules, such as:

- dealers in securities or currencies;
- traders in securities that elect to use a mark-to-market method of accounting for securities holdings;
- banks or certain financial institutions;
- insurance companies;
- tax-exempt organizations;
- partnerships or other entities treated as partnerships or other pass-through entities for U.S. federal income tax purposes or persons holding ADSs or ordinary shares through any such entities;
- regulated investments companies or real estate investment trusts;
- persons that hold ADSs or ordinary shares as part of a hedge, straddle, constructive sale, conversion transaction or other integrated investment;
- persons whose functional currency for tax purposes is not the U.S. dollar;
- persons liable for alternative minimum tax; or
- persons who actually or constructively own 10% or more of the total combined voting power of all classes of our shares entitled to vote (including ADSs and ordinary shares).

This discussion is based on the U.S. Internal Revenue Code of 1986, as amended, which we refer to in this discussion as the Code, its legislative history, existing and proposed regulations promulgated thereunder, published rulings and court decisions, all as of the date hereof. These laws are subject to change, possibly on a retroactive basis. In addition, this discussion relies on our assumptions regarding the value of our ADSs and ordinary shares and the nature of our business over time. Finally, this discussion is based in part, upon representations of the depositary and the assumptions that each obligation in the deposit agreement and any related agreement will be performed in accordance with its terms.

**Prospective purchasers are urged to consult their own tax advisor concerning the particular U.S. federal income tax consequences to them of the purchase, ownership and disposition of our ADSs and ordinary shares, as well as the consequences to them arising under the laws of any other taxing jurisdiction.**

For purposes of the U.S. federal income tax discussion below, you are a “U.S. Holder” if you beneficially own ADSs or ordinary shares as capital assets within the meaning of Section 1221 of the Code and are:

- a citizen or resident of the United States for U.S. federal income tax purposes;
- a corporation, or other entity taxable as a corporation, that was created or organized in or under the laws of the United States or any state thereof or the District of Columbia;
- an estate the income of which is subject to U.S. federal income tax regardless of its source; or
- a trust if (a) a court within the United States is able to exercise primary supervision over its administration and one or more U.S. persons have the authority to control all substantial decisions of the trust, or (b) the trust has a valid election in effect to be treated as a U.S. person.

For U.S. federal income tax purposes, income earned through a U.S. or non-U.S. partnership or other flow-through entity is attributed to its owners. Accordingly, if a partnership or other flow-through entity holds ADSs or ordinary shares, the tax treatment of the holder will depend on the status of the partner or other owner and the activities of the partnership or other flow-through entity.

### **Dividends on ADSs and ordinary shares**

Subject to the “Passive Foreign Investment Company” discussion below, if we make distributions and you are a U.S. Holder, the gross amount of any distributions with respect to your ADSs and ordinary shares (including the amount of any taxes withheld therefrom) will be includible in your gross income on the day you actually or constructively receive such income as dividend income if the distributions are made from our current or accumulated earnings and profits, calculated according to U.S. federal income tax principles. With respect to non-corporate U.S. Holders, certain dividends received in taxable years beginning before January 1, 2013 from a qualified foreign corporation may be subject to a reduced rate of taxation. A non-U.S. corporation is treated as a qualified foreign corporation with respect to dividends from that corporation on shares (or ADSs backed by such shares) that are readily tradable on an established securities market in the United States. U.S. Treasury Department guidance indicates that our ADSs, which are listed on NYSE, but not our ordinary shares, will be readily tradable on an established securities market in the United States. You should consult your own tax advisor as to the rate of tax that will apply to you with respect to dividend distributions, if any, you receive from us.

Subject to the “Passive Foreign Investment Company” discussion below, to the extent, if any, that the amount of any distribution by us on ADSs and ordinary shares exceeds our current and accumulated earnings and profits as determined under U.S. federal income tax principles, it will be treated first as a tax-free return of the U.S. Holder’s adjusted tax basis in the ADSs and ordinary shares and thereafter as capital gain. However, we do not intend to calculate our earnings and profits according to U.S. federal income tax principles. Accordingly, distributions on our ADSs and ordinary shares, if any, will generally be reported to you as dividend distributions for U.S. tax purposes. Corporations will not be entitled to claim a dividends-received deduction with respect to distributions made by us. Dividends may constitute foreign source passive income for purposes of the U.S. foreign tax credit rules. You should consult your own tax advisors as to your ability, and the various limitations on your ability, to claim foreign tax credits in connection with the receipt of dividends.

### **Sales and other dispositions of ADSs or ordinary shares**

Subject to the “Passive Foreign Investment Company” discussion below, when you sell or otherwise dispose of ADSs or ordinary shares, you will recognize capital gain or loss in an amount equal to the difference between the amount realized on the sale or other disposition and your adjusted tax basis in the ADSs or ordinary shares. Any such gain or losses that you recognize will be treated as U.S. source income for foreign tax credit limitation purposes. Your adjusted tax basis will equal the amount you paid for the ADSs or ordinary shares. Any gain or loss you recognize will be long-term capital gain or loss if your holding period in our ADSs or ordinary shares is more than one year at the time of disposition. If you are a non-corporate U.S. Holder, including an individual, any such long-term capital gain will be taxed at preferential rates. Your ability to deduct capital losses will be subject to various limitations.

### **Passive foreign investment company**

In general, we will be classified as a PFIC in any taxable year if either: (a) the average quarterly value of our gross assets that produce passive income or are held for the production of passive income is at least 50% of the average quarterly value of our total gross assets or (b) 75% or more of our gross income for the taxable year is passive income (such as certain dividends, interest or royalties). For purposes of the first test: (a) any cash and cash invested in short-term, interest-bearing, debt instruments or bank deposits that are readily convertible into cash will generally count as producing passive income or held for the production of passive income, and (b) the total value of our assets is calculated based on our market capitalization.

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 stock.

We believe that we were not a passive foreign investment company, or PFIC, for U.S. federal income tax purposes for our taxable year ended September 30, 2011. However, the application of the PFIC rules is subject to ambiguity in several respects, and, in addition, PFIC status is tested each year and depends on the composition of our assets and income and the value of our assets from time to time. Since we currently hold, and expect to continue to hold, a substantial amount of cash and other passive assets and, since the value of our assets is to be determined in large part by reference to the market prices of our ADSs and ordinary shares, which is likely to fluctuate over time, there can be no assurance that we will not be a PFIC in the current taxable year or in any future taxable year.

If we were a PFIC for any taxable year during which you held ADSs or ordinary shares, certain adverse U.S. federal income tax rules would apply. You would generally be subject to additional taxes and interest charges on certain “excess distributions” we make and on any gain realized on the disposition or deemed disposition of your ADSs or ordinary shares, regardless of whether we continue to be a PFIC in the year in which you receive an “excess distribution” or dispose of or are deemed to have disposed of, your ADSs or ordinary shares. Distributions in respect of your ADSs or ordinary shares during a taxable year would generally constitute “excess distributions” if, in the aggregate, they exceed 125% of the average amount of distributions with respect to your ADSs or ordinary shares over the three preceding taxable years or, if shorter, the portion of your holding period before such taxable year.

To compute the tax on “excess distributions” or any gain, (a) the “excess distribution” or the gain would be allocated ratably to each day in your holding period, (b) the amount allocated to the current year and any tax year prior to the first taxable year in which we were a PFIC would be taxed as ordinary income in the current year, (c) the amount allocated to other taxable years would be taxable at the highest applicable marginal rate in effect for that year, and (d) an interest charge at the rate for underpayment of taxes for any period described under (c) above would be imposed on the resulting tax liability on the portion of the “excess distribution” or gain that is allocated to such period. In addition, if we were a PFIC, no distribution that you receive from us would qualify for taxation at the preferential rate discussed in the “Dividends on ADSs or ordinary shares” section above.

Under certain attribution rules, if we are a PFIC, you will be deemed to own your proportionate share of lower-tier PFICs, and will be subject to U.S. federal income tax on (i) a distribution on the shares of a lower-tier PFIC and (ii) a disposition of shares of a lower-tier PFIC, both as if you directly held the shares of such lower-tier PFIC.

If we were a PFIC in any year, as a U.S. Holder, you may be required to file an annual return on IRS Form 8621 regarding your ADSs and ordinary shares. In addition, under newly enacted legislation, unless otherwise provided by the U.S. Treasury, each U.S. shareholder of a PFIC is required to file an annual report containing such information as the U.S. Treasury may require. If we are or become a PFIC, you should consult with your tax adviser regarding reporting requirements with regard to your ADSs and ordinary shares. If we were a PFIC in any year, you would generally be able to avoid the “excess distribution” rules described above by making a timely “mark-to-market” election with respect to your ADSs provided our ADSs are “marketable.” Our ADSs will be “marketable” as long as they remain regularly traded on a national securities exchange, such as the NYSE. If you made this election in a timely fashion, you would generally recognize as ordinary income or ordinary loss the difference between the fair market value of your ADSs on the first day of any taxable year and their value on the last day of that taxable year. Any ordinary income resulting from this election would generally be taxed at ordinary income rates and would not be eligible for the reduced rate of tax applicable to qualified dividend income. Any ordinary losses would be limited to the extent of the net amount of previously included income as a result of the mark-to-market election, if any. Your basis in the ADSs would be adjusted to reflect any such income or loss. You should consult your own tax advisor regarding potential advantages and disadvantages to you of making a “mark-to-market” election with respect to your ADSs. The mark-to-market election will not be available for any lower tier PFIC that is deemed owned pursuant to the attribution rules discussed above.

Alternatively, a U.S. Holder of stock in a PFIC may make a so-called “Qualified Electing Fund” election to avoid the PFIC rules regarding “excess” distribution and gain described above. A U.S. Holder that makes such an election would include in income for a taxable year its pro rata share of the corporation’s income for the taxable year. However, we do not intend to provide you with the information you would need to make or maintain a “Qualified Electing Fund” election and you will, therefore, not be able to make or maintain such an election with respect to your ADSs or ordinary shares.

## **U.S. information reporting and backup withholding rules**

Dividend payments with respect to the ADSs and ordinary shares and the proceeds received on the sale or other disposition of ADSs and ordinary shares may be subject to information reporting to the IRS and to backup withholding (currently imposed at a rate of 28%). Backup withholding will not apply, however, if you (a) are a corporation or come within certain other exempt categories and, when required, can demonstrate that fact or (b) provide a taxpayer identification number, certify as to no loss of exemption from backup withholding and otherwise comply with the applicable backup withholding rules. To establish your status as an exempt person, you will be required to provide certification on IRS Form W-9. Any amounts withheld from payments to you under the backup withholding rules that exceed your U.S. federal income tax liability will be allowed as a refund or a credit against your U.S. federal income tax liability, provided that you furnish the required information to the IRS. Under newly enacted legislation, certain individuals holding the ADSs or ordinary shares other than in an account at a U.S. financial institution may be subject to additional information reporting requirements.

PROSPECTIVE PURCHASERS OF OUR ADSS AND ORDINARY SHARES SHOULD CONSULT THEIR OWN TAX ADVISOR REGARDING THE APPLICATION OF THE U.S. FEDERAL INCOME TAX LAWS TO THEIR PARTICULAR SITUATIONS AS WELL AS ANY TAX CONSEQUENCES RESULTING FROM PURCHASING, HOLDING OR DISPOSING OF OUR ADSS AND ORDINARY SHARES, INCLUDING THE APPLICABILITY AND EFFECT OF THE TAX LAWS OF ANY STATE, LOCAL OR NON-US JURISDICTION AND INCLUDING ESTATE, GIFT AND INHERITANCE LAWS.

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

Not applicable.

### **G. Statement by Experts.**

Not applicable.

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

We previously filed with the Securities and Exchange Commission our registration statement on Form F-1 as amended.

We have filed this annual report on Form 20-F with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Statements made in this annual report as to the contents of any document referred to are not necessarily complete. With respect to each such document filed as an exhibit to this annual report, reference is made to the exhibit for a more complete description of the matter involved, and each such statement shall be deemed qualified in its entirety by such reference.

We are subject to the informational requirements of the Exchange Act and file reports and other information with the Securities and Exchange Commission. Reports and other information which we filed with the Securities and Exchange Commission, including this annual report on Form 20-F, may be inspected and copied at the public reference room of the Securities and Exchange Commission at 100 F Street, N.E. Washington D.C. 20549.

You can also obtain copies of this annual report on Form 20-F by mail from the Public Reference Section of the Securities and Exchange Commission, 100 F Street, N.E., Washington D.C. 20549, at prescribed rates. Additionally, copies of this material may be obtained from the Securities and Exchange Commission's Internet site at <http://www.sec.gov>. The Commission's telephone number is 1-800-SEC-0330.

### **I. Subsidiary Information**

For a listing of our subsidiaries, see "Item 4. Information on the Company — C. Organizational Structure."

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

### **Quantitative and Qualitative Disclosures about Market Risk**

#### ***Interest Rate Risk***

Our exposure to interest rate risk primarily relates to our interest income generated by excess cash, which is mostly held in interest-bearing bank deposits and AAA rated money market funds, as of the date of this annual report. We have not used derivative financial instruments in our investment portfolio. We have not been exposed, nor do we anticipate being exposed, to material risks due to changes in market interest rates. However, our future interest income may fall short of expectations due to changes in market interest rates.



## ***Foreign Currency Risk***

Substantially all of our revenues and expenditures are denominated in Renminbi. As a result, fluctuations in the exchange rate between the U.S. dollars and Renminbi will affect our financial results in U.S. dollars terms without giving effect to any underlying change in our business or results of operations. The Renminbi's exchange rate with the U.S. dollar and other currencies is affected by, among other things, changes in China's political and economic conditions and China's foreign exchange policies. The People's Bank of China regularly intervenes in the foreign exchange market to limit fluctuations in Renminbi exchange rate and achieve certain exchange rate targets, and through such intervention kept the U.S. dollar-Renminbi exchange rate relatively stable between 6.8 and 6.9 Renminbi per U.S. dollar for almost two years from July 2008. On June 20, 2010, the People's Bank of China announced that the PRC government would further reform the Renminbi exchange rate regime and increase the flexibility of the exchange rate. Under China's current exchange rate regime, the Renminbi may appreciate or depreciate significantly in value against the U.S. dollar in the medium to long term. There remains significant international pressure on the PRC government to adopt a substantial liberalization of its currency policy, which could result in a further and more significant appreciation in the value of the Renminbi against the U.S. dollar.

To the extent that we need to convert our U.S. dollar denominated cash balance into Renminbi for our operations, appreciation of the Renminbi against the U.S. dollar would have an adverse effect on the Renminbi amount we receive from the conversion. Assuming we had converted the U.S. dollar denominated cash balance of \$34.2 million as of September 30, 2011 into Renminbi at the exchange rate of \$1.00 for RMB6.3780 as of September 30, 2011, this cash balance would have been RMB217.8 million. Assuming a further 1.0% appreciation of the Renminbi against the U.S. dollar, this cash balance would have decreased to RMB215.6 million as of September 30, 2011.

Very limited hedging transactions are available in China to reduce our exposure to exchange rate fluctuations. 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 availability and effectiveness of these hedging transactions may be limited and we may not be able to successfully hedge our exposure at all. In addition, our currency exchange losses may be magnified by PRC exchange control regulations that restrict our ability to convert Renminbi into foreign currency.

## **ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

### **A. Debt Securities.**

Not applicable.

### **B. Warrants and Rights.**

Not applicable.

### **C. Other Securities.**

Not applicable.

### **D. American Depositary Shares.**

#### **Fees and Charges Payable by a Holder of American Depositary Receipts**

Persons depositing shares are charged a fee for each issuance of ADSs, including issuances resulting from distributions of shares, share dividends, share splits, exercise of rights, bonus and rights distributions and other property, and for each surrender of ADSs in exchange for deposited securities. The fee in each case is US\$5.00 for each 100 ADSs, or any portion thereof, issued or surrendered. The depositary also charges a fee of US\$2.00 per 100 ADSs for distribution of cash proceeds pursuant to a cash distribution, sale of rights and other entitlements or otherwise. The depositary may also charge an annual fee of US\$2.00 per 100 ADSs for the operation and maintenance costs in administering the facility. Persons depositing shares also may be charged the following expenses:

- Expenses incurred by the depositary, the custodian or their respective agents in connection with inspections of the relevant share register maintained by the local registrar and/or performing due diligence on the central securities depository: an annual fee of U.S.\$1.00 per 100 ADSs (such fee to be assessed against holders of record as at the date or dates set by the depositary as it sees fit and collected at the discretion of the depositary, subject to the Company's prior consent, by billing such holders for such fee or by deducting such fee from one or more cash dividends or other cash distributions)
- Taxes and other governmental charges incurred by the depositary or the custodian on any ADR or ordinary shares underlying an ADR, including any applicable interest and penalties thereon, and any share transfer or other taxes and other governmental charges

- Cable, telex, electronic transmission and delivery expenses
- Transfer or registration fees for the registration of transfer of deposited securities on any applicable register in connection with the deposit or withdrawal of deposited securities including those of a central depository for securities (where applicable)
- Expenses of the depository in connection with the conversion of foreign currency into U.S. dollars
- Fees and expenses incurred by the depository in connection with compliance with exchange control regulations and other regulatory requirements applicable to the shares, deposited securities and ADSs; and
- Any other fees, charges, costs or expenses that may be incurred by the depository from time to time

In the case of cash distributions, fees are generally deducted from the cash being distributed. Service fees may be collected from holders of ADSs in a manner determined by the depository with respect to ADSs registered in the name of investors (whether certificated or in book-entry form) and ADSs held in brokerage and custodian accounts (via DTC). In the case of distributions other than cash (i.e., stock dividends, rights, etc.), the depository charges the applicable ADS record date holder concurrent with the distribution. In the case of ADSs registered in the name of the investor (whether certificated or in book-entry form), the depository sends invoices to the applicable record date ADS holders.

In the case of ADSs held in brokerage and custodian accounts (via DTC), the depository may, if permitted by the settlement systems provided by DTC, collect the fees through such settlement systems (whose nominee is the registered holder of the ADSs held in DTC) from the brokers and custodians holding ADSs in their DTC accounts. The brokers and custodians who hold their clients' ADSs in DTC accounts in such case may in turn charge their clients' accounts the amount of the service fees paid to the depository.

In the event of refusal to pay the service fee, the depository may, under the terms of the deposit agreement, refuse the requested service until payment is received or may set off the amount of the service fee from any distribution to be made to the ADS holder.

If any tax or other governmental charge is payable by the holders and/or beneficial owners of ADSs to the depository, the depository, the custodian or the Company may withhold or deduct from any distributions made in respect of deposited securities and may sell for the account of the holder and/or beneficial owner any or all of the deposited securities and apply such distributions and sale proceeds in payment of such taxes (including applicable interest and penalties) or charges, with the holder and the beneficial owner thereof remaining fully liable for any deficiency.

#### **Fees and Other Direct and Indirect Payments Made by the Depository**

Since the commencement of the Company's most recent fiscal year, the Company has received the following direct and indirect payments in the amounts of \$0.04 million for expenses incurred by the Company relating to the ADR program, including:

- Roadshow expenses
- Production of annual reports and Form 20-F filings
- Postage for mailing annual and interim reports and other communications to ADR holders
- Costs of retaining third party public relations, investor relations, and/or corporate communications advisory firms in the U.S.
- Participation in retail investor shows and capital markets days

## **PART II**

### **ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

None.

### **ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS**

On August 16, 2010, we entered into a restricted issuance agreement with Duetsche Bank Trust Company Americas, as depository, pursuant to which the depository may issue restricted American depository shares upon a deposit of restricted securities by a depositor. Other than the foregoing, the rights of securities holders have not been materially modified.

## **ITEM 15. CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our chief executive officer and chief financial officer, has performed an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this report, as required by Rule 13a-15(b) under the Exchange Act. Based on that evaluation, our chief executive officer and chief financial officer has concluded that, as of September 30, 2011, our disclosure controls and procedures were effective to ensure that the information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that the information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our chief executive officer and chief financial officer, to allow timely decisions regarding required disclosure.

### **Management's Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) under the Exchange Act. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements in accordance with generally accepted accounting principles, and includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of a company's assets, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that a company's receipts and expenditures are being made only in accordance with authorizations of a company's management and directors, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of a company's assets that could have a material effect on the consolidated 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 and procedures may deteriorate.

As required by Section 404 of the Sarbanes-Oxley Act and related rules as promulgated by the SEC, our management, with the participation of our chief executive officer and our chief financial officer, evaluated the effectiveness of our internal control over financial reporting based on criteria established in the framework in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, our management has concluded that our internal control over financial reporting was effective as of September 30, 2011.

Our independent registered public accounting firm has audited our internal control over financial reporting as of September 30, 2011 and has issued an attestation report set forth below.

### **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders of China Distance Education Holdings Limited

We have audited the internal control over financial reporting of China Distance Education Holdings Limited (the "Company"), its subsidiaries, its variable interest entity and the subsidiaries of its variable interest entity (collectively, the "Group") as of September 30, 2011, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Group's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Group's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of September 30, 2011, based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended September 30, 2011 of the Group and our report dated February 28, 2012 expressed an unqualified opinion on those financial statements.

/s/ Deloitte Touche Tohmatsu CPA Ltd,  
Beijing, the People's Republic of China  
February 28, 2012

#### **Changes in Internal Control over Financial Reporting**

There were no significant changes in our internal control over financial reporting during the year ended September 30, 2011 that have materially affected, or a reasonably likely to materially affect, our internal control over financial reporting.

#### **ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT**

Our audit committee consists of Carol Yu, Liankui Hu and Xiaoshu Chen. Carol Yu is the chairman of our audit committee. Our board of directors has determined that all of our audit committee members satisfy the "independence" requirements of relevant rules of the NYSE and Rule 10A-3 under the Securities Exchange Act of 1934. Carol Yu meets the criteria of an audit committee financial expert as set forth under the applicable rules of the SEC.

#### **ITEM 16B. CODE OF ETHICS**

Our board of directors has adopted a code of ethics that is applicable to our senior executive and financial officers. In addition, our board of directors adopted a code of conduct that is applicable to all of our directors, officers and employees. Our code of ethics and our code of conduct are publicly available on our website, <http://www.cdeledu.com>.

#### **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 Deloitte Touche Tohmatsu CPA Ltd., or Deloitte, our principal external auditors, in the fiscal year ended September 30, 2010 and 2011, respectively.

	Fiscal Year ended September 30,			
	2010		2011	
	RMB	US\$	RMB	US\$
Audit fees (1)	3,208,798	471,882	3,272,974	487,932
Audit-related fees (2)	1,791,202	263,118	1,827,026	272,068
Tax fees (3)	—	—	—	—

(1) "Audit fees" means the aggregate fees billed or payable for professional services rendered by our independent auditors in connection with the audit of our consolidated financial statements or the review of our interim consolidated financial statements required for statutory or regulatory filings.

- (2) “Audit-related fees” means the aggregate fees billed or payable for professional services rendered by our independent auditors in connection with the review of our interim consolidated financial statements not required for statutory or regulatory filings.
- (3) “Tax fees” means the aggregate fees billed or payable for tax compliance services, transfer pricing and requests for rulings or technical advice from taxing authorities and tax planning services.

The audit committee or our board of directors is to pre-approve all auditing services and permitted non-audit services to be performed for us by our independent registered public accounting firm, including the fees and terms thereof (subject to the de minimis exceptions for non-audit services described in Section 10A(i)(1)(B) of the Exchange Act which are approved by the audit committee or our board of directors prior to the completion of the audit).

#### **ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES**

None.

#### **ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS**

The table below details our purchases of our own equity securities pursuant to our share repurchase program adopted and publicly announced on November 20, 2008 and extended in November 2009, November 2010, April 2011 and February 2012, respectively. In addition, on April 29, 2011, the board of directors approved an increase of the repurchase quota under the share repurchase program. The expanded share repurchase program authorizes the repurchase of up to an additional \$10 million of our ADSs (which makes the total repurchase quota under the share repurchase program \$20 million ADSs) and would be valid until April 28, 2012. On February 28, 2012, the board of directors decided to further extend the share repurchase program for 12 months until April 28, 2013. As of December 31, 2011, we have repurchased a total of 3,603,017 ADSs, representing 14,412,068 ordinary shares, in open-market transactions for total cash consideration of \$14.2 million. See “Item 5.B. Operating and Financial Review and Prospects — Liquidity and Capital Resources” for a further discussion of the repurchase program.

<u>Period</u>	<u>Total Number of ADSs Purchased</u>	<u>Average Price Paid Per ADS</u>	<u>Total Number of ADSs Purchased as Part of Publicly Announced Program</u>	<u>Approximate Dollar Value of ADSs that May Yet be Purchased Under the Program</u>
10/1/2010 – 10/31/2010	20,820	5.1414	20,820	\$ 3.8 million
11/1/2010 – 11/30/2010	6,100	5.1237	6,100	\$ 3.8 million
12/1/2010 – 12/31/2010	13,900	4.4354	13,900	\$ 3.7 million
01/01/2011 – 01/31/2011	64,200	4.6723	64,200	\$ 3.4 million
02/01/2011 – 02/28/2011	91,500	4.4697	91,500	\$ 3.0 million
03/01/2011 – 03/31/2011	89,100	3.9907	89,100	\$ 2.7 million
04/01/2011 – 04/30/2011	443,680	3.4016	443,680	\$ 1.2 million
05/01/2011 – 05/31/2011	1,077,884	3.4220	1,077,884	\$ 7.4 million
06/01/2011 – 06/30/2011	62,113	2.8431	62,113	\$ 7.2 million
07/01/2011 – 07/31/2011	68,173	2.6084	68,173	\$ 7.0 million
08/01/2011 – 08/31/2011	385,667	2.8979	385,667	\$ 5.9 million
09/01/2011 – 09/30/2011	7,660	2.3905	7,660	\$ 5.9 million

#### **ITEM 16F. CHANGE IN REGISTRANT’S CERTIFYING ACCOUNTANT**

None.

#### **ITEM 16G. CORPORATE GOVERNANCE**

As a foreign private issuer with ADSs listed on the NYSE we are subject to corporate governance requirements imposed by the NYSE. Under Section 303A of the NYSE Listed Company Manual, in general NYSE-listed non-U.S. companies may follow their home-country corporate governance practices in lieu of some of the NYSE corporate governance requirements. We are committed to a high standard of corporate governance. As such, we strive to comply with most of the NYSE corporate governance practices. However, the following are the ways in which our current corporate governance practices differ from NYSE corporate governance requirements because the laws of Cayman Islands do not require such compliance:

- We are not required to obtain shareholder approval for the adoption of, or material revisions to, our equity-compensation plans where our directors consider it in the best interests of the company to do so and when the issue price of shares issued pursuant to such plans is otherwise fair.
- Our compensation committee of our board of directors is not comprised entirely of independent directors.

- Our nomination committee of our board of directors is not comprised entirely of independent directors.

We may determine to voluntarily comply with one or more of the foregoing provisions as required by the NYSE Listed Company Manual.

### PART III

#### ITEM 17. FINANCIAL STATEMENTS

We have elected to provide our financial statements pursuant to Item 18.

#### ITEM 18. FINANCIAL STATEMENTS

Our consolidated financial statements are included at the end of this annual report.

#### ITEM 19. EXHIBITS

##### Index to Exhibits

<u>Exhibit No.</u>	<u>Description of Exhibit</u>
1.1	—Form of Second Amended and Restated Memorandum of Association and Articles of Association of the Registrant*
2.1	—Form of Ordinary Share Certificate.*
2.2	—Form of Deposit Agreement between the Registrant and Deutsche Bank Trust Company Americas, as depositary. <sup>(1)</sup>
2.3	—Form of American depositary receipt evidencing American depositary shares (included in Exhibit 2.2). <sup>(1)</sup>
2.4	—Restricted Issuance Agreement between the Registrant and Deutsche Bank Trust Company Americas, as depositary, dated August 16, 2010. ***
4.1	—Technical Support and Consultancy Services Agreement between Beijing Champion Distance Education Technology Co., Ltd. and Beijing Champion Hi-Tech Co., Ltd., dated May 1, 2004.*
4.2	—Equity Pledge Agreement between Beijing Champion Distance Education Technology Co., Ltd and Zhengdong Zhu, dated May 1, 2004.*
4.3	—Equity Pledge Agreement between Beijing Champion Distance Education Technology Co., Ltd. and Baohong Yin, dated May 1, 2004.*
4.4	—Exclusive Purchase Rights Agreement among China Distance Education Limited, Beijing Champion Hi-Tech Co., Ltd. and Zhengdong Zhu, dated May 9, 2004.*
4.5	—Exclusive Purchase Rights Agreement among China Distance Education Limited, Beijing Champion Hi-Tech Co., Ltd. and Baohong Yin, dated May 9, 2004.*
4.6	—Courseware License Agreement between Beijing Champion Hi-Tech Co., Ltd. and Beijing Champion Distance Education Technology Co., Ltd., dated August 1, 2004.*
4.7	—Software License Agreement between Beijing Champion Education Technology Co., Ltd. and Beijing Champion Hi-Tech Co., Ltd., dated May 20, 2007.*
4.8	—Courseware Production Entrustment Agreement between Beijing Champion Education Technology Co., Ltd. and Beijing Champion Hi-Tech Co., Ltd., dated May 20, 2007.*
4.9	—Letter of Undertaking from Beijing Champion Distance Education Technology Co., Ltd. to Beijing Champion Hi-Tech Co., Ltd., dated February 13, 2008.*
4.10	—Letter of Undertaking from Zhengdong Zhu and Baohong Yin to Beijing Champion Distance Education Technology Co., Ltd., dated February 13, 2008.*
4.11	—Declaration Letter by Zhengdong Zhu, dated March 24, 1008.*
4.12	—Declaration Letter by Baohong Yin, dated March 24, 2008.*
4.13	—Power of Attorney by Zhengdong Zhu, dated March 25, 2008.*

<u>Exhibit No.</u>	<u>Description of Exhibit</u>
4.14	—Power of Attorney by Baohong Yin, dated March 25, 2008.*
4.15	—Notice from Beijing Champion Distance Education Technology Co., Ltd. to Beijing Champion Hi-Tech Co., Ltd., Zhengdong Zhu and Baohong Yin, dated March 25, 2008.*
4.16	—Acknowledgement Letter from Zhengdong Zhu and Baohong Yin to the Registrant, dated March 25, 2008.*
4.17	—Acknowledgement Letter from Zhengdong Zhu and Baohong Yin to Beijing Champion Distance Education Technology Co., Ltd., dated March 25, 2008.*
4.18	—Shareholders Agreement among the Registrant, China Distance Education Limited, Beijing Champion Distance Education Technology Co., Ltd., Beijing Champion Education Technology Co., Ltd., Beijing Champion Hi-Tech Co., Ltd., Champion Shine Trading Limited, Empire China Limited, Zhengdong Zhu, Hongfeng Sun, Baohong Yin, Orchid Asia III, L.P., Orchid Asia Co-Investment Limited, and Artson Limited, dated March 7, 2008, as amended on July 25, 2008.*
4.19	—Form confidentiality and non-competition agreement.*
4.20	—Incentive share plan.*
4.21	—2008 Performance Incentive Plan.*
4.22	—Amended and Restated 2008 Performance Incentive Plan. **
4.23	—Amended and Restated Equity Pledge Agreement between Beijing Champion Distance Education Technology Co., Ltd. and Zhengdong Zhu, dated December 31, 2008. **
4.24	—Amended and Restated Equity Pledge Agreement between Beijing Champion Distance Education Technology Co., Ltd. and Baohong Yin, dated December 31, 2008. **
8.1	—Subsidiaries of Registrant.***
11.1	—Code of Business Conduct and Ethics of the Registrant.*
12.1	—CEO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
12.2	—CFO Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
13.1	—CEO Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
13.2	—CFO Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
15.1	—Consent of Deloitte Touche Tohmatsu CPA Ltd.
15.2	—Consent of Jingtian & Gongcheng.
15.3	—Consent of American Appraisal.

\* Previously filed with the Registrant's registration statement on Form F-1 (File No. 333-152167), as amended.

\*\* Previously filed with the Registrant's Annual Report on Form 20-F for the year ended September 30, 2008.

\*\*\* Previously filed with the Registrant's Annual Report on Form 20-F for the year ended September 30, 2011.

\*\*\*\* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

(1) Incorporated by reference to the Registration Statement on Form F-6 (File No. 333-152345) filed with the Securities and Exchange Commission with respect to American depository shares representing our ordinary shares.





**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**  
**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

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## **REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**TO THE BOARD OF DIRECTORS AND STOCKHOLDERS OF  
CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

We have audited the accompanying consolidated balance sheets of China Distance Education Holdings Limited, its subsidiaries, its variable interest entity and the subsidiaries of variable interest entity (collectively, the “Group”) as of September 30, 2010 and 2011, and the related consolidated statements of operation, changes in equity and comprehensive income (loss), and cash flows for each of the three years in the period ended September 30, 2011. These consolidated financial statements are the responsibility of the Group’s management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Group as of September 30, 2010 and 2011, and the results of its operation and its cash flow for each of the three years in the period ended September 30, 2011, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Group’s internal control over financial reporting as of September 30, 2011, based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 28, 2012 expressed an unqualified opinion on the Group’s internal control over financial reporting.

/s/ Deloitte Touche Tohmatsu CPA Ltd.  
Beijing, the People’s Republic of China  
February 28, 2012

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share and per share data)

	As of September 30,	
	2010 US\$	2011 US\$
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	57,305	49,738
Term deposits	—	7,839
Restricted cash	2,906	2,676
Accounts receivable, net of allowance for doubtful accounts of US\$2,236 and US\$3,190 as of September 30, 2010 and September 2011, respectively	4,012	4,661
Inventories	599	363
Prepayment and other current assets	2,039	2,861
Deferred tax assets, current portion	1,016	1,556
Deferred cost	1,596	1,868
Current assets of discontinued operations	4,626	2,306
<b>Total current assets</b>	<b>74,099</b>	<b>73,868</b>
<b>Non-current assets</b>		
Property, plant and equipment, net	8,082	8,586
Goodwill	7,024	7,403
Other intangible assets, net	2,757	2,382
Purchased call options	1,083	—
Deposit for purchase of non-current assets	—	242
Deferred tax assets, non-current portion	153	668
Other non-current assets	744	729
Long-term assets of discontinued operations	2,029	—
<b>Total non-current assets</b>	<b>21,872</b>	<b>20,010</b>
<b>Total assets</b>	<b>95,971</b>	<b>93,878</b>
<b>LIABILITIES AND EQUITY</b>		
<b>Current liabilities</b>		
Accrued expenses and other liabilities (including accrued expenses and other liabilities of the consolidated VIE without recourse to China Distance Education Holdings Limited of US\$3,174 and US\$5,738 as of September 30, 2010 and September 30, 2011, respectively)	3,822	6,514
Income tax payable (including income tax payable of the consolidated VIE without recourse to China Distance Education Holdings Limited of US\$1,518 and US\$2,170 as of September 30, 2010 and September 30, 2011, respectively)	1,586	2,329
Deferred revenue (including deferred revenue of the consolidated VIE without recourse to China Distance Education Holdings Limited of US\$7,545 and US\$7,848 as of September 30, 2010 and September 30, 2011, respectively)	7,545	7,861
Refundable fees (including refundable fees of the consolidated VIE without recourse to China Distance Education Holdings Limited of US\$1,564 and US\$2,580 as of September 30, 2010 and September 30, 2011, respectively)	1,564	2,580
Current liabilities of discontinued operations (including current liabilities of discontinued operations of the consolidated VIE without recourse to China Distance Education Holdings Limited of US\$4,295 and US\$1,860 as of September 30, 2010 and September 30, 2011, respectively)	4,295	1,860
<b>Total current liabilities</b>	<b>18,812</b>	<b>21,144</b>

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**CONSOLIDATED BALANCE SHEETS - continued**  
(In thousands, except share and per share data)

	As of September 30,	
	2010	2011
	US\$	US\$
<b>Non-current liabilities</b>		
Non-current liabilities of discontinued operations (including non-current liabilities of discontinued operations of the consolidated VIE without recourse to China Distance Education Holdings Limited of US\$136 and nil as of September 30, 2010 and September 30, 2011, respectively)	136	—
<b>Total non-current liabilities</b>	136	—
<b>Total liabilities</b>	18,948	21,144
<b>Commitments and contingencies (Note 20)</b>		
<b>Equity</b>		
Ordinary shares (par value of US\$0.0001 per share at September 30, 2010 and 2011, respectively; Authorized - 480,000,000 shares at September 30, 2010 and 2011; Issued and outstanding - 136,932,849 and 127,800,673 shares at September 30, 2010 and 2011, respectively)	14	13
Additional paid-in capital	79,075	78,804
Accumulated other comprehensive income	2,399	4,221
Cumulative deficits	(6,502)	(10,304)
<b>Total China Distance Education Holdings Limited shareholders' equity</b>	74,986	72,734
<b>Non-controlling interest-continuing operations</b>	1,126	—
<b>Non-controlling interest-discontinued operations</b>	911	—
<b>Total equity</b>	77,023	72,734
<b>Total liabilities and equity</b>	95,971	93,878

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

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except share and per share data)

	Years ended September 30,		
	2009	2010	2011
	US\$ Adjusted (Note 4, 17)	US\$ Adjusted (Note 4)	US\$
<b>Sales, net of business tax, value-added tax and related surcharges</b>			
Online education services	22,279	23,982	30,788
Books and reference materials	2,709	3,939	4,743
Others	5,133	4,658	6,033
<b>Total net revenues</b>	<u>30,121</u>	<u>32,579</u>	<u>41,564</u>
<b>Cost of sales</b>			
Cost of services	(12,834)	(13,283)	(16,840)
Cost of tangible goods sold	(1,577)	(2,070)	(2,794)
<b>Total cost of sales</b>	<u>(14,411)</u>	<u>(15,353)</u>	<u>(19,634)</u>
<b>Gross profit</b>	15,710	17,226	21,930
<b>Operating expenses</b>			
Selling expenses	(6,722)	(7,176)	(9,771)
General and administrative expenses	(7,432)	(10,535)	(12,221)
Impairment of purchased call options	—	(162)	(1,115)
<b>Total operating expenses</b>	<u>(14,154)</u>	<u>(17,873)</u>	<u>(23,107)</u>
Other operating income	292	74	603
<b>Operating income (loss)</b>	1,848	(573)	(574)
Interest income	740	458	883
Exchange loss	(6)	(66)	(143)
<b>Income (loss) before income taxes</b>	2,582	(181)	166
Less: Income tax expense	(1,478)	(575)	(971)
<b>Net income (loss) from continuing operations</b>	1,104	(756)	(805)
Net loss of continuing operations attributable to noncontrolling interest	82	911	303
<b>Net income (loss) from continuing operations attributable to China Distance Education Holdings Limited</b>	1,186	155	(502)
<b>Net income (loss) from discontinued operations attributable to China Distance Education Holdings Limited, net of tax</b>	2	(2,053)	(3,300)
<b>Net income (loss) attributable to China Distance Education Holdings Limited</b>	<u>1,188</u>	<u>(1,898)</u>	<u>(3,802)</u>
<b>Net (loss) income per share:</b>			
<b>Net (loss) income attributable to China Distance Education Holdings Limited shareholders</b>			
Basic from continuing operations	0.01	—	—
Basic from discontinued operations (net of tax)	—	(0.01)	(0.03)
<b>Basic</b>	<u>0.01</u>	<u>(0.01)</u>	<u>(0.03)</u>
Diluted from continuing operations	0.01	—	—
Diluted from discontinued operations (net of tax)	—	(0.01)	(0.03)
<b>Diluted</b>	<u>0.01</u>	<u>(0.01)</u>	<u>(0.03)</u>
<b>Weighted average shares used in calculating net (loss) income per share</b>			
Basic	140,260,811	138,232,493	133,571,727
<b>Diluted</b>	<u>140,475,941</u>	<u>138,232,493</u>	<u>133,571,727</u>

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

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
**AND COMPREHENSIVE INCOME (LOSS)**  
(In thousands, except share data)

	China Distance Education Holding Limited shareholders								
	Number of ordinary shares	Ordinary shares US\$	Additional paid-in capital US\$	Accumulated other comprehensive income US\$	Cumulative deficits US\$	Total China Distance Education Holding Limited shareholders' equity US\$	Noncontrolling interest US\$	Total equity US\$	Total Comprehensive income (loss) for the year US\$
Balance as of September 30, 2008 (Note 17)	141,897,737	14	76,811	1,717	(5,792)	72,750	—	72,750	
Net income (loss) for the year	—	—	—	—	1,188	1,188	(82)	1,106	1,106
Foreign currency translation adjustments	—	—	—	(15)	—	(15)	(2)	(17)	(17)
Repurchase of ordinary shares	(3,163,600)	—	(3,960)	—	—	(3,960)	—	(3,960)	1,089
Options exercised	31,548	—	26	—	—	26	—	26	
Stock-based compensation expense - stock options (Note 23)	—	—	3,920	—	—	3,920	—	3,920	
Noncontrolling interest arising from acquisition of start-up training business	—	—	—	—	—	—	2,110	2,110	
Noncontrolling interest arising from acquisition of Gaokao retake preparation and high-school supplementary tutoring services ("Gaokao retake business")	—	—	—	—	—	—	937	937	
Balance as of September 30, 2009	138,765,685	14	76,797	1,702	(4,604)	73,909	2,963	76,872	
Net loss for the year	—	—	—	—	(1,898)	(1,898)	(944)	(2,842)	(2,842)
Foreign currency translation adjustments	—	—	—	697	—	697	18	715	715
Repurchase of ordinary shares	(1,909,600)	—	(2,172)	—	—	(2,172)	—	(2,172)	(2,127)
Options exercised	76,764	—	63	—	—	63	—	63	
Stock-based compensation expense - stock options (Note 23)	—	—	4,387	—	—	4,387	—	4,387	
Balance as of September 30, 2010	136,932,849	14	79,075	2,399	(6,502)	74,986	2,037	77,023	
Net loss for the year	—	—	—	—	(3,802)	(3,802)	(303)	(4,105)	(4,105)
Foreign currency translation adjustments	—	—	—	1,822	—	1,822	33	1,855	1,855
Repurchase of ordinary shares	(9,223,188)	(1)	(8,137)	—	—	(8,138)	—	(8,138)	(2,250)
Options exercised	91,012	—	75	—	—	75	—	75	
Stock-based compensation expense - stock options (Note 23)	—	—	6,024	—	—	6,024	—	6,024	
Acquisition of noncontrolling Interest of Gaokao retake business (Note 3)	—	—	911	—	—	911	(911)	—	
Acquisition of noncontrolling Interest of start-up training business (Note 3)	—	—	856	—	—	856	(856)	—	
Balance as of September 30, 2011	127,800,673	13	78,804	4,221	(10,304)	72,734	—	72,734	

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

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	Years ended September 30,		
	2009 US\$ (Note 17)	2010 US\$	2011 US\$
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income (loss)	1,106	(2,842)	(4,105)
Adjustments to reconcile net (loss) income to net cash provided by operating activities:			
Stock-based compensation	3,920	4,387	6,024
Depreciation of property, plant and equipment	930	1,157	1,449
Amortization of other intangible assets	579	851	926
Provision of inventories	3	(1)	1
Allowance for doubtful accounts	—	2,197	1,144
Impairment loss on purchased call option	—	639	1,316
Impairment loss on intangible assets	—	274	332
Impairment loss on property, plant and equipment	—	—	973
Impairment loss on goodwill	—	1,407	758
Losses on disposition of property, plant and equipment	—	44	27
Changes in operating assets and liabilities:			
Increase in accounts receivable	(4,323)	(1,970)	(17)
(Increase) decrease in inventories	(123)	(289)	258
Increase in prepayments and other assets	(112)	(693)	(1,054)
Decrease (increase) in deferred tax assets	1,505	(352)	(630)
Increase in deferred cost	(841)	(276)	(189)
(Increase) decrease in other non-current assets	(808)	79	50
Increase in accrued expenses and other liabilities	805	1,850	1,111
(Decrease) increase in income tax payable	(89)	719	622
Increase (decrease) in deferred revenue	2,137	1,037	(235)
(Decrease) increase in refundable fees	(2,907)	(249)	917
Decrease in deferred tax liabilities	(175)	(316)	(486)
Net cash generated from operating activities	<u>1,607</u>	<u>7,653</u>	<u>9,192</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Acquisition of business (net of cash acquired of US\$2,854 respectively for the year ended September 30, 2009)	(3,211)	(21)	—
Maturity (purchase) of term deposits	(27,753)	27,750	(7,649)
Withdrawal (deposit) of restricted cash	(8,250)	5,395	363
Acquisition of property, plant and equipment	(1,451)	(1,570)	(1,999)
Proceeds from disposition of property, plant and equipment	—	60	80
Acquisition of other intangible assets	(513)	(194)	(402)
Payment of deposit for the acquisition of non-current assets	(356)	—	(236)
Net cash (used in) generated from investing activities	<u>(41,534)</u>	<u>31,420</u>	<u>(9,843)</u>

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS - continued**  
(In thousands)

	Years ended September 30,		
	2009 US\$ (Note 17)	2010 US\$	2011 US\$
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Repurchase of ordinary shares	(3,960)	(2,172)	(8,138)
Proceeds from share options exercised by employees	26	63	75
Payment of deferred initial public offering costs	(907)	—	—
Net cash used in financing activities	<u>(4,841)</u>	<u>(2,109)</u>	<u>(8,063)</u>
Exchange rate effect on cash and cash equivalents	(18)	354	906
Net (decrease) increase in cash and cash equivalents	(44,786)	37,318	(7,808)
Cash and cash equivalents at beginning of the year	66,223	21,437	58,755
Cash and cash equivalents at end of the year	<u>21,437</u>	<u>58,755</u>	<u>50,947</u>
Supplemental schedule of cash flows information			
Income tax paid	(334)	(514)	(1,439)
Supplemental schedule of non-cash activities			
Payable for acquisition of property, plant and equipment included in accrued expenses and other liabilities	—	94	633
Acquisition of property, plant and equipment and other intangible assets through utilization of deposits	151	356	—
Consideration payable in connection with acquisition of Champion Xinlixiang	1,628	1,643	—
Offset consideration payable in connection with acquisition of Champion Xinlixiang with receivable from original selling shareholder	<u>—</u>	<u>—</u>	<u>(1,711)</u>

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



**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
(In thousands, except share and per share data)

**1. ORGANIZATION AND BASIS OF PRESENTATION**

China Distance Education Holdings Limited (the “Company”) was incorporated under the law of the Cayman Islands on January 11, 2008. The Company, its subsidiaries, its consolidated variable interest entity (“VIE”) and VIE’s subsidiaries (collectively the “Group”) are primarily engaged in providing online and offline education services, and selling related products in the People’s Republic of China (“PRC”).

As of September 30, 2011, details of the Company’s subsidiaries and variable interest entities were as follows:

<u>Company</u>	<u>Date of establishment</u>	<u>Place of establishment</u>	<u>Percentage of legal ownership by the Company</u>	<u>Principal activities</u>
<b>Subsidiaries:</b>				
China Distance Education Limited (“CDEL Hong Kong”) Practice Enterprises Network	March 13, 2003	Hong Kong	100%	Investment holding
China International Links Limited (“Pencil”) Beijing Champion Distance Education Technology Co., Ltd. (“Champion Technology”)	February 23, 2010	Hong Kong	100%	Inactive
Beijing Champion Education Technology Co., Ltd. (“Champion Education Technology”)	January 5, 2004	PRC	100%	Provision of technical support and consultancy services and course production
Beijing Champion Education Technology Co., Ltd. (“Champion Education Technology”)	April 23, 2007	PRC	100%	Software licensing and course production
<b>Variable interest entity:</b>				
Beijing Champion Hi-Tech Co., Ltd. (“Beijing Champion”)	July 12, 2000	PRC	Nil	Provision of online education services and sales of books and reference materials
<b>Subsidiaries of variable interest entity:</b>				
Beijing Caikaowang Company Ltd. (“Caikaowang”)	November 28, 2007	PRC	Nil	Provision of online education services
Beijing Champion Wangge Education Technology Co., Ltd. (“Champion Wangge”)	June 24, 2008	PRC	Nil	Provision of online education services
Beijing Zhengbao Yucai Education Technology Co., Ltd. (“Zhengbao Yucai”)	February 19, 2009	PRC	Nil	Provision of start-up training services
Beijing Haidian District Champion Training School (“Champion Training School”)	February 19, 2009	PRC	Nil	Provision of online and offline education services
Zhejiang Champion Xinlixiang Education Management Co., Ltd. (“Champion Xinlixiang”) (i)	July 8, 2009	PRC	Nil	Provision of Gaokao retake related education services

(i) In September 2011, the Group decided to dispose 100% of Champion Xinlixiang as stated in Note 4 Discontinued Operations.

***The VIE arrangements***

Applicable PRC laws and regulations prohibit foreign investors from providing telecommunications value-added services in the PRC. As a Cayman Islands corporation, the Company is deemed a foreign legal person under PRC laws.

To comply with these foreign ownership restrictions, the Company operates its online education services through the VIE, Beijing Champion, and VIE’s subsidiaries in the PRC. To provide the Company effective control over the VIE and the ability to receive substantially all of the economic benefits of the VIE and its subsidiaries, a series of contractual arrangements were entered into amongst CDEL Hong Kong, Champion Technology, Beijing Champion and Beijing Champion’s direct equity holders.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
**(In thousands, except share and per share data)**

**1. ORGANIZATION AND BASIS OF PRESENTATION - continued**

*The VIE arrangements - continued*

- Agreements that transfer economic benefits to Champion Technology

*Exclusive technical support and consultancy services agreement*

Pursuant to the exclusive technical support and consultancy services agreement between Beijing Champion and Champion Technology, Champion Technology has the exclusive right to provide to Beijing Champion technical and consulting services. Champion Technology is entitled to charge Beijing Champion a service fee equal to its profit before such service fee and tax. This agreement will remain effective until Beijing Champion ceases its operations.

*Exclusive purchase right agreement on the equity interest of Beijing Champion*

Pursuant to the exclusive purchase right agreement, CDEL Hong Kong may purchase the entire equity interest in, or all the assets of Beijing Champion, for a purchase price equal to the net assets of Beijing Champion or the minimum price permitted by PRC laws, if and when PRC laws are amended to permit such a transaction. The term of this agreement is ten years from the date thereof and can be extended for another ten years at the discretion of CDEL Hong Kong.

*Letter of undertaking from Beijing Champion's shareholders to Champion Technology*

Pursuant to this letter addressed to Champion Technology, the shareholders of Beijing Champion undertook to, unless restricted by laws, regulations or legal procedures, (i) remit all dividends, interests, other distributions or remnant assets after liquidation, if any, they receive from Beijing Champion to Champion Technology without compensation, after paying the corresponding tax and any other required expenses, (ii) transfer all or part of their equity interests to CDEL Hong Kong at a nominal or minimal purchase price, in the event CDEL Hong Kong exercises its exclusive purchase right to acquire any or all of the equity interests in Beijing Champion, (iii) remit to Champion Technology all considerations they may receive from CDEL Hong Kong's acquisition of any equity interests in Beijing Champion, without compensation, after paying the corresponding tax and any other required expenses and (iv) act in the best interest of Champion Technology.

CHINA DISTANCE EDUCATION HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)

1. ORGANIZATION AND BASIS OF PRESENTATION - continued

*The VIE arrangements - continued*

- Agreements that provide Company effective control over Beijing Champion

*Equity pledge agreement*

Pursuant to the equity pledge agreement between Beijing Champion and Champion Technology, the equity holders of Beijing Champion have pledged their equity interest in Beijing Champion to Champion Technology to secure the payment obligations of Beijing Champion under the technical support and consultancy services agreement between Beijing Champion and Champion Technology. This agreement will remain effective until the discharge of Beijing Champion's contractual obligations under the exclusive technical support and consultancy services agreement as described above.

*Power of attorney*

Pursuant to the power of attorney, the nominee shareholders of Beijing Champion each executed an irrevocable power of attorney assigning Champion Technology or any person designated by Champion Technology as their attorney-in-fact to vote on their behalf on all matters of Beijing Champion requiring shareholder approval under PRC laws and regulations and the articles of association of Beijing Champion.

The Articles of Incorporation of Beijing Champion states that the major rights of the shareholders include the power to review and approve annual budget, operating strategy and investment plan, elect the members of board of directors and approve their compensation plan. Therefore, through the irrevocable power of attorney arrangement, Champion Technology has the ability to exercise effective control over Beijing Champion through equity holder votes and, through such votes, to also control the composition of the board of directors. In addition, the senior management team of Beijing Champion is the same as that of Champion Technology.

These contractual arrangements allow the Group to effectively control Beijing Champion and its subsidiaries and to derive substantially all of the economic benefits from them. Accordingly, the Group treats Beijing Champion as a VIE and because the Group is the primary beneficiary of Beijing Champion, the Group has consolidated the financial results of Beijing Champion and its subsidiaries.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
**(In thousands, except share and per share data)**

**1. ORGANIZATION AND BASIS OF PRESENTATION - continued**

*The VIE arrangements - continued*

However, there are certain risks related to the VIE arrangements, which include but are not limited to the following:

- If the ownership structure and contractual arrangements are found to be in violation of any existing or future PRC laws or regulations, the Group could be subject to severe penalties;
- The Group rely on contractual arrangements with the VIE and its shareholders for substantially all of its China operations, which may not be as effective as direct ownership in providing operational control; and
- The Group may have to incur significant cost to enforce, or may not be able to effectively enforce, the contractual arrangements with the VIE and its shareholders in the event of a breach or non-compliance by the VIE or its shareholders.

In June 2009, the FASB issued an authoritative pronouncement to amend the accounting rules for variable interest entities. The amendments effectively replace the quantitative-based risks-and-rewards calculation for determining which reporting entity, if any, has a controlling financial interest in a variable interest entity with an approach focused on identifying which reporting entity has (1) the power to direct the activities of a variable interest entity that most significantly affect the entity's economic performance and (2) the obligation to absorb losses of, or the right to receive benefits from, the entity. Additionally, an enterprise is required to assess whether it has an implicit financial responsibility to ensure that a variable interest entity operates as designed when determining whether it has the power to direct the activities of the variable interest entity that most significantly impact the entity's economic performance. The new guidance also requires additional disclosures about a reporting entity's involvement with variable interest entities and about any significant changes in risk exposure as a result of that involvement.

The guidance is effective at the start of a reporting entity's first fiscal year beginning after November 15, 2009, and all interim and annual periods thereafter.

Since the Company, through its subsidiary, has (1) the power to direct the activities of the VIE that most significantly affect the VIE's economic performance and (2) the right to receive benefits from the VIE, the Company continued to consolidate the VIE upon the adoption of the new guidance on October 1, 2010, which therefore, other than for additional disclosures, has no accounting impact.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
(In thousands, except share and per share data)

**1. ORGANIZATION AND BASIS OF PRESENTATION - continued**

*The VIE arrangements - continued*

The following financial information of the Company's VIE and VIE's subsidiaries as of September 30, 2010 and 2011 and for each of the three years in the period ended September 30, 2011 was included in the accompanying consolidated financial statements after elimination of intercompany transactions and balances within VIE and VIE's subsidiaries:

	<u>As of September 30,</u>	
	<u>2010</u>	<u>2011</u>
	US\$	US\$
Total assets	41,247	40,679
Total liabilities	29,779	27,198

	<u>For the years ended</u>		
	<u>September 30,</u>		
	<u>2009</u>	<u>2010</u>	<u>2011</u>
	US\$	US\$	US\$
Revenues	29,722	33,257	42,510
Net income (1)	10,824	6,370	7,365
Net cash provided by operating activities	3,314	6,614	2,860
Net cash used in investing activities	(4,431)	(4,407)	(2,137)

(1) This is net income before service fees charged by Champion Technology and Champion Education Technology.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)**

**2. SIGNIFICANT ACCOUNTING POLICIES**

*Basis of presentation and use of estimates*

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the balance sheet dates and the reported amounts of revenues and expenses during the reporting periods. Significant estimates and assumptions reflected in the Group's financial statements include, but are not limited to, revenue recognition, fair value of purchased call option, deferred tax assets valuation allowance, uncertain tax positions, allowance for doubtful accounts, impairment of goodwill and long-term assets, and share-based compensation expenses. Actual results could materially differ from those estimates.

Certain accounts and balances in the 2009 and 2010 financial statements and the related notes have been retrospectively adjusted to reflect the effect of discontinued operations as described in Note 4.

*Principles of consolidation*

The consolidated financial statements include the financial statements of the Company, its subsidiaries, its VIE and VIE's subsidiaries. All transactions and balances among the Company, its subsidiaries, its VIE and VIE's subsidiaries have been eliminated upon consolidation.

*Foreign currency translation and transactions*

The Company, CDEL Hong Kong and PENCIL's functional currencies are United States dollars ("US\$"). The Company's PRC subsidiaries, VIE and VIE's subsidiaries determine their functional currencies to be the Chinese Renminbi ("RMB"). The Company uses the US\$ as its reporting currency and uses the monthly average exchange rate for the year and the exchange rate at the balance sheet date to translate the operating results and financial position of its PRC subsidiaries and its variable interest entities, respectively. Translation differences are recorded in accumulated other comprehensive income, a component of consolidated statements of changes in equity and comprehensive income (loss).

Transactions denominated in foreign currencies are remeasured into the functional currency at the exchange rates prevailing on the transaction dates. Foreign currency denominated financial assets and liabilities are remeasured at the balance sheet date exchange rate. Exchange gains and losses are included in the consolidated statements of operations.

*Cash and cash equivalents*

Cash and cash equivalents consist of cash on hand and highly liquid investments which are unrestricted as to withdrawal or use, and which have an original maturity of three months or less when purchased.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)**

**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Term deposits*

Term deposits consist of deposits placed with financial institutions with an original maturity of greater than three months and less than one year.

*Restricted cash*

Restricted cash as of September 30, 2010 and 2011 were US\$2,906 and US\$2,676, representing the cash deposit in a designated account as required by court for the arbitration process in relation to Zhengbao Yucai (see note 3). The restriction was subsequently removed in November 2011 upon the settlement of the arbitration.

*Inventories*

Inventories, consisting of papers and professional examination reference books, are stated at the lower of cost or market value. Cost is determined using the first in, first out method.

*Fair value*

Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Group considers the principal or most advantageous market in which it would transact and it considers assumptions that market participants would use when pricing the asset or liability. Authoritative literature provides a fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The level in the hierarchy within which the fair value measurement in its entirety falls is based upon the lowest level of input that is significant to the fair value measurement as follows:

*Level 1*

Level 1 applies to assets or liabilities for which there are quoted prices in active markets for identical assets or liabilities.

*Level 2*

Level 2 applies to assets or liabilities for which there are inputs other than quoted prices included within Level 1 that are observable for the asset or liability such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which significant inputs are observable or can be derived principally from, or corroborated by, observable market data.

*Level 3*

Level 3 applies to assets or liabilities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities.

CHINA DISTANCE EDUCATION HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)

2. SIGNIFICANT ACCOUNTING POLICIES - continued

*Allowance for doubtful accounts*

An allowance for doubtful accounts is recorded in the period in which a loss is determined to be probable based on an assessment of specific evidence indicating doubtful collection, historical experience, account balance aging and prevailing economic conditions. Accounts receivable balances are written off after all collection efforts have been exhausted.

*Property, plant and equipment, net*

Property, plant and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the assets, as follows:

<u>Category</u>	<u>Estimated useful life</u>	<u>Estimated residual value</u>
Buildings	35 years	5-10%
Electronic and office equipment	5 years	5-10%
Motor vehicles	5 years	5-10%
Leasehold improvement and building improvement	Shorter of lease term or 5 years	—

Repair and maintenance costs are charged to expense as incurred, whereas the cost of renewals and betterment that extends the useful lives of property, plant and equipment are capitalized as additions to the related assets. Retirements, sales and disposals of assets are recorded by removing the cost and accumulated depreciation from the asset and accumulated depreciation accounts with any resulting gain or loss reflected in the consolidated statements of operations.

*Goodwill*

The excess of the purchase price over the fair value of net assets acquired is recorded on the consolidated balance sheet as goodwill. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired. Goodwill is tested following a two-step process. The first step compares the fair value of a reporting unit to its carrying amount, including goodwill. If the fair value of each reporting unit exceeds its carrying amount, goodwill is not considered to be impaired and the second step will not be required. If the carrying amount of a reporting unit exceeds its fair value, the second step will be performed to compare the implied fair value of goodwill to the carrying value of a reporting unit's goodwill. The implied fair value of goodwill is determined in a manner similar to accounting for a business combination with the allocation of the assessed fair value determined in the first step to the assets and liabilities of the reporting unit. The excess of the fair value of the reporting unit over the amounts assigned to the assets and liabilities is the implied fair value of goodwill. An impairment loss is recognized for any excess in the carrying value of goodwill over the implied fair value of goodwill.



CHINA DISTANCE EDUCATION HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)

2. SIGNIFICANT ACCOUNTING POLICIES - continued

*Other intangible assets, net*

Other intangible assets are amortized using the straight-line basis over the estimated useful lives as follows:

<u>Category</u>	<u>Estimated useful life</u>
Computer software	3~5 years
Domain names and trademarks	10~11 years
Courseware	1~5 years
Website	5 years
Business contracts	3~5 years
Copyrights	5 years
Platform	3.5 years
Non-compete agreement	15 years

*Impairment of long-lived assets*

The Group evaluates its long-lived assets or asset group including intangibles with definite lives for impairment whenever events or changes in circumstances (such as a significant adverse change to market conditions that will impact the future use of the assets) indicate that the carrying amount of a group of long-lived assets may not be fully recoverable. When these events occur, the Group evaluates the impairment by comparing the carrying amount of the assets to future undiscounted net cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected undiscounted cash flows is less than the carrying amount of the assets, the Group recognizes an impairment loss based on the excess of the carrying amount of the asset group over its fair value, generally based upon discounted cash flows.

If the intent is to hold the asset for sale and certain other criteria are met (i.e., the asset can be disposed of currently, appropriate levels of authority have approved sale, and there is an actively pursuing buyer), the impairment test is a comparison of the asset's carrying value to its fair value less costs to sell. To the extent that the carrying value is greater than the asset's fair value less costs to sell, an impairment loss is recognized for the difference. Assets held for sale are separately presented on the balance sheet and are no longer depreciated.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 2. SIGNIFICANT ACCOUNTING POLICIES - continued

##### *Revenue recognition*

Revenues are recognized when the following four criteria are met: (i) persuasive evidence of an arrangement exists, (ii) the service has been rendered, (iii) the fees are fixed or determinable, and (iv) collectability is reasonably assured.

##### *Online education services*

The online education service provided by the Group to its customers is an integrated service, including audio-video course content, mock examinations and online chat rooms during the subscription period. Audio-video course content, mock examinations and online chat rooms are not practical to be sold on standalone basis and have never been sold separately.

The Group earns revenues by providing online education services to customers pursuant to two types of revenue models - non-refundable course model and refundable course model. For online courses using the non-refundable course model, revenues are recognized on a straight line basis over the subscription period from the month in which the customers enroll in the courses to the month in which subscribed courses terminate. For online courses using the refundable course model, if the customers complete the courses and fail the professional exams and their scores are within a range provided for in the agreement, they are entitled to either a full refund or the right to retake the course. The customers must notify the Group within a 15-day period after the professional examinations scores are released in order to be eligible for the refund or the right to retake the course. The proceeds from the refundable course model are initially recorded as "refundable fees". Revenues are recognized upon the expiration of the customers' right to receive a refund or ratably over the course period if the customer decides to retake the course before the expiration of such right.

Customers enroll for online courses mainly through the use of prepaid study cards which are purchased from distributors. The Group sells to its distributors prepaid study cards at a discount to the face value of the cards. Revenues are recorded using the after-discount-selling-price of the cards and recognized over the period the online course is available to the customer, which generally is from the enrollment date to the completion of the relevant professional examination date. Sales of prepaid study cards that are not activated for course enrollment are recognized as revenues upon expiration of the cards. Prepaid study cards that have been activated but have not been used to enroll online courses do not have an expiry date and will be deferred until they are used to enroll in online courses. Customers who enroll with the Company directly are eligible to a refund within a 7-day trial period. Revenues from direct enrollment with the Company are recognized over the period from the lapse of the 7-day trial period to the completion of the relevant professional examination date.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
**(In thousands, except share and per share data)**

**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Revenue recognition - continued*

*Online education services - continued*

The Group may, at times, offer volume discounts to its distributors for purchases over a specified amount of prepaid cards during a specified period of time, generally, one year. The amount of future rebates relating to these volume discounts cannot be reasonably estimated and accordingly a deferred revenue balance is recognized for the maximum potential amount of volume discount. If the number of purchases specified in the volume discount provisions is not reached upon the expiry of the volume discount period, the deferred revenue relating to such volume discount for each study card is recognized as revenue over the remaining period the online course is available to the user who enrolls using the study card or recognized as revenue immediately if the related online course has been completed. Proceeds allocated to the rebate study cards that have never been activated for course enrollment are recognized as revenues upon expiration of the cards.

For the years ended September 30, 2009, 2010 and 2011, the Group recognized revenues before business tax and related surcharges in connection with expired study cards amounted to US\$90, US\$90 and US\$103 respectively.

The online service is provided by Beijing Champion and its subsidiaries which are subject to approximately 3% business tax and related surcharges. The Group records revenues net of these taxes in the consolidated statement of operations. Such business tax and related surcharges for the years ended September 30, 2009, 2010 and 2011 were US\$1,014, US\$777 and US\$918 respectively.

*Books and reference materials*

The Group sells books and reference materials to distributors and end users. Revenues relating to such sales are deferred until cash is collected. Inventory costs of products delivered to distributors for which revenues have been deferred are presented as “deferred costs” on the consolidated balance sheets.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Revenue recognition - continued*

*Books and reference materials - continued*

The Group also sells books and reference materials together with study cards which allow the customers to take a certain number of on-line courses for no additional charge. These sales are considered arrangements with two deliverables, consisting of the delivery of books and reference material and the on-line courses service.

In October 2009, the FASB published FASB ASU 2009-13, Revenue Recognition (Topic 605) - Multiple-Deliverable Revenue Arrangements. The guidance establishes a selling price hierarchy for determining the selling price of a deliverable, which is based on: (a) vendor-specific objective evidence if available (“VSOE”); (b) third-party evidence (“TPE”) if vendor-specific objective is not available; or (c) estimated selling price (“ESP”) if neither vendor-specific objective evidence nor third-party evidence is available. The guidance required disclosures on how the application of the relative selling price method affects the timing and amount of revenue recognition. The Group prospectively adopted the guidance for multiple elements arrangements entered into on or after October 1, 2010 and allocates revenue to each deliverables based on their relative selling price. The adoption of the new guidance did not have a material impact on the Group’s financial statements.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Revenue recognition - continued*

*Other revenues*

Other revenues include sales of offline education services, courseware production services, platform production services, and others.

Revenues from offline training are recognized when the training courses are provided. For offline training sponsored by government authorities, the tuition fees of the training participants are subsidized by the government. Qualified enrollments and the fees to be earned cannot be determined until the confirmation from government authorities regarding the number of students and fees is received by the Company, which is after the completion of services. Therefore, revenues from such services are recognized upon cash receipt or the receipt of confirmations from government authorities, whichever is earlier.

Revenues from sales of courseware, which are designed and developed pursuant to the requests from customers, are recognized when the courseware or platforms are accepted by the customers. The Company has no significant remaining obligation with respect to the courseware or platforms upon the acceptance of the customers.

From time to time, the Group enters into arrangement to provide the development and maintenance of online platforms to its customers. After the development of online platforms, the Group provides support and maintenance services. The development of online platform and the support and maintenance services have never been sold separately and they do not have standalone value to the customers. Accordingly, revenues from such arrangement is accounted as a single unit of accounting and recognized ratably over the support and maintenance services period.

Revenues from other services, including magazine content production, advertising and consulting services, are recognized over the period when such services are provided.

*Value added taxes*

The Group is subject to PRC value added tax ("VAT") generally at a rate of 13% on proceeds received from customers for sales related to books and reference materials, which reduces revenues, and are entitled to an offset for VAT paid for the books and reference materials as well as a portion of VAT paid related to purchase of fixed assets. Net VAT balance between input VAT and output VAT is recorded in either other current liabilities or other current assets on the consolidated balance sheets.

*Cost of sales*

Cost of online education services primarily includes the production costs of study cards, server and bandwidth leasing fees, lecturer fees, staff costs involved in the operation of online education services including network operation and maintenance, course production and tutor services and other direct costs of providing these services. These costs are expensed when incurred.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Cost of sales - continued*

The cost of books and reference materials, including direct materials used for production of books, authorship fee and printing cost, are initially deferred and recorded as “deferred cost”. The deferred costs are recognized as cost of sales when the related revenue is recognized upon cash receipt.

5% business tax on technical and consulting service, software licensing and course production fees that Champion Technology and Champion Education Technology charge Beijing Champion is included in the cost of services.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Advertising expenditure*

Advertising expenditure is expensed when incurred and are included in “selling expenses” in the consolidated statements of operations. Advertising expenses from continuing operations were US\$1,997, US\$1,123 and US\$2,204, and those from discontinued operations were nil, US\$132 and US\$179, for the years ended September 30, 2009, 2010 and 2011, respectively.

*Shipping and handling costs*

Shipping and handling costs of books and reference materials are classified as a component of “selling expenses” in the consolidated statements of operations. Shipping and handling costs classified as selling expenses from continuing operations were US\$382, US\$327 and US\$330, and those from discontinued operations were nil, US\$4 and US\$8, for the years ended September 30, 2009, 2010 and 2011, respectively.

*Income taxes*

Current income taxes are provided for in accordance with the laws of the relevant tax authorities. Deferred income taxes are recognized when temporary differences exist between the tax bases of assets and liabilities and their reported amounts in the financial statements. Net operating loss carry forwards and credits are applied using enacted statutory tax rates applicable to future years. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more-likely-than-not that a portion of or all of the deferred tax assets will not be realized. The components of the deferred tax assets and liabilities are individually classified as current and non-current based on their characteristics. The impact of an uncertain income tax position is recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant tax authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Interest and penalties on income taxes will be classified as a component of the provisions for income taxes.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Share-based compensation*

Share-based compensation with employees is measured based on the grant-date fair value of the equity instrument issued and recognized as compensation expense over the requisite service period, with a corresponding addition to paid-in capital. The Group recognizes compensation expense over the vesting term on a straight-line basis with the amount of compensation expense recognized at any date not less than the portion of the grant-date value of the option vested at that date.

Share-based compensation with non-employee is measured based on the fair value of options at the earlier of the performance commitment date or the date at which the non-employee's performance is complete (hereafter referred to as the measurement date). The Group recognizes compensation expense using the graded vesting attribution method.

Share-based compensation awards which require the issuance of a variable number of shares to settle a fixed monetary amount are accounted for as liabilities.

*Net income per share*

Basic net income per share is computed by dividing income attributable to holders of ordinary shares by the weighted average number of ordinary shares outstanding during the period. Nonvested restricted shares are also participating securities as they enjoy identical dividend rights as ordinary shares. Accordingly, the Group uses the two-class method whereby undistributed net income is allocated on a pro rata basis to each participating share to the extent that each class may share in income for the period. Diluted net income per share reflects the potential dilution that could occur if securities or other contracts to issue ordinary shares were exercised or converted into ordinary shares. The dilutive effect of outstanding share-based awards is reflected in the diluted net income per share by application of the treasury stock method.



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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

***Business combinations***

Business combinations are recorded using the purchase method of accounting. On October 1, 2009, the Group adopted a new accounting pronouncement with prospective application which made certain changes to the previous authoritative literature on business combinations. From October 1, 2009, the assets acquired, the liabilities assumed, and any noncontrolling interest of the acquiree at the acquisition date, if any, are measured at their fair values as of that date. Goodwill is recognized and measured as the excess of the total consideration transferred plus the fair value of any noncontrolling interest of the acquiree, if any, at the acquisition date over the fair values of the identifiable net assets acquired. Previously, any non-controlling interest was reflected at historical cost. Common forms of the consideration made in acquisitions include cash and common equity instruments. Consideration transferred in a business acquisition is measured at the fair value as at the date of acquisition.

Where the consideration in an acquisition includes contingent consideration the payment of which depends on the achievement of certain specified conditions post-acquisition, from October 1, 2009 the contingent consideration is recognized and measured at its fair value at the acquisition date and if recorded as a liability it is subsequently carried at fair value with changes in fair value reflected in earnings. For periods prior to October 1, 2009 contingent consideration was not recorded until the contingency was resolved.

In addition, upon the adoption of the accounting pronouncement regarding noncontrolling interests (see note 17), from October 1, 2009, changes in a parent's ownership interest while the parent retains its controlling financial interest in its subsidiary are accounted for as equity transaction. Therefore, no gain or loss would be recognized and any difference between the fair value of the consideration received or paid and the amount by which the noncontrolling interest is adjusted is recognized in equity to the parent.

***Comprehensive income (loss)***

Comprehensive income (loss) includes net income and foreign currency translation adjustments. Comprehensive income (loss) is reported as a component of the consolidated statements of changes in equity and comprehensive income (loss).

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**2. SIGNIFICANT ACCOUNTING POLICIES - continued**

*Significant Risks and Uncertainties*

*Foreign currency risk*

RMB is not a freely convertible currency. The State Administration for Foreign Exchange, under the authority of the People's Bank of China, controls the conversion of RMB into foreign currencies. The value of RMB is subject to changes in central government policies and to international economic and political developments affecting supply and demand in the China Foreign Exchange Trading System market. The cash and cash equivalents of the Group including the continuing operations and discontinued operations included aggregate amounts of US\$15,802 and US\$16,716, which were denominated in RMB, at September 30, 2010 and 2011, respectively, representing 26.9% and 32.8% of the cash and cash equivalents at September 30, 2010 and 2011, respectively.

*Concentration of credit risk*

Financial instrument that potentially expose the Group to significant concentration of credit risk primarily consist of cash and cash equivalents, accounts receivable and funds receivable. As of September 30, 2011, substantially all of the Group's cash and cash equivalents were deposited in financial institutions located in the PRC and Hong Kong. Accounts receivable are typically unsecured and are derived from revenue earned from customers in the PRC. The risk with respect to accounts receivable is mitigated by credit evaluations the Group performs on its customers and its ongoing monitoring process of outstanding balances. Funds receivable are unsecured and are held by external payment networks who collect fees from customers through online payment networks. The funds are transferred to the Group within one to three business days after payments are received by external payment networks. To mitigate the credit risk, the Group only engages large scale and reputable payment networks to collect fees on its behalf. The Group also monitors the timeliness and accuracy of funds transfer by the external payment networks and the credit worthiness of the external payment networks.

There are no revenues from customers which individually represent greater than 10% of the total net revenues for any year of the three years period ended September 30, 2011.

Primarily due to the long payment cycles of government agencies, the Group had two customers that accounted for 11.5% and 24.9% of the Group's accounts receivable balances as of September 30, 2010, respectively, and two customers that accounted for 28.4% and 12.6% of the Group's accounts receivable balances as of September 30, 2011, respectively.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 2. SIGNIFICANT ACCOUNTING POLICIES - continued

##### *Recently issued accounting pronouncements*

In May 2011, the Financial Accounting Standard Board (“FASB”) issued an authoritative pronouncement on fair value measurement. The guidance is the result of joint efforts by the FASB and International Accounting Standards Board to develop a single, converged fair value framework. The guidance is largely consistent with existing fair value measurement principles in US GAAP. The guidance expands the existing disclosure requirements for fair value measurements and makes other amendments, mainly including:

- Highest-and-best-use and valuation-premise concepts for nonfinancial assets – the guidance indicates that the highest-and-best-use and valuation-premise concepts only apply to measuring the fair value of nonfinancial assets.
- Application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk – the guidance permits an exception to fair value measurement principles for financial assets and financial liabilities (and derivatives) with offsetting positions in market risks or counterparty credit risk when several criteria are met. When the criteria are met, an entity can measure the fair value of the net risk position.
- Premiums or discounts in fair value measure – the guidance provides that premiums or discounts that reflect size as a characteristic of the reporting entity’s holding (specifically, a blockage factor that adjusts the quoted price of an asset or a liability because the market’s normal daily trading volume is not sufficient to absorb the quantity held by the entity) rather than as a characteristic of the asset or liability (for example, a control premium when measuring the fair value of a controlling interest) are not permitted in a fair value measurement.
- Fair value of an instrument classified in a reporting entity’s stockholders’ equity – the guidance prescribes a model for measuring the fair value of an instrument classified in stockholders’ equity; this model is consistent with the guidance on measuring the fair value of liabilities.
- Disclosures about fair value measurements – the guidance expands disclosure requirements, particularly for Level 3 inputs. Required disclosures include:
  - (i) For fair value measurements categorized in Level 3 of the fair value hierarchy: (1) a quantitative disclosure of the unobservable inputs and assumptions used in the measurement, (2) a description of the valuation process in place (e.g., how the entity decides its valuation policies and procedures, as well as changes in its analyses of fair value measurements, from period to period), and (3) a narrative description of the sensitivity of the fair value to changes in unobservable inputs and interrelationships between those inputs.
  - (ii) The level in the fair value hierarchy of items that are not measured at fair value in the statement of financial position but whose fair value must be disclosed.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 2. SIGNIFICANT ACCOUNTING POLICIES - continued

##### *Recently issued accounting pronouncements - continued*

The guidance is to be applied prospectively and is effective for interim and annual periods beginning after December 15, 2011, for public entities. Early application by public entities is not permitted. The Group does not expect the adoption of this guidance to have a significant effect on its consolidated financial statements.

In June 2011, the FASB issued an authoritative pronouncement to require an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The guidance does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The guidance should be applied retrospectively. For public entities, the guidance is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. The Group does not expect the adoption of this guidance to have a significant effect on its consolidated financial statements.

In September 2011, the FASB issued an authoritative pronouncement related to testing goodwill for impairment. The guidance is intended to simplify how entities, both public and nonpublic, test goodwill for impairment. The guidance permits an entity to first assess qualitative factors to determine whether it is "more likely than not" that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. The guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if a public entity's financial statements for the most recent annual or interim period have not yet been issued. The Group does not expect the adoption of this pronouncement to have a significant impact on its financial condition or results of operations.

In December 2011, the FASB issued an authoritative pronouncement related to Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update. This guidance allows the FASB to redeliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. While the FASB is considering the operational concerns about the presentation requirements for reclassification adjustments and the needs of financial statement users for additional information about reclassification adjustments, entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before update the pronouncement issued in June 2011. The Group does not expect the adoption of this guidance to have a significant effect on its consolidated financial statements.

In December 2011, the FASB has issued an authoritative pronouncement related to Disclosures about Offsetting Assets and Liabilities. The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. The Group does not expect the adoption of this pronouncement to have a significant impact on its financial condition or results of operations.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 3. ACQUISITIONS

##### *Acquisition of Zhengbao Yucai*

On March 10, 2009, Beijing Champion acquired the business of start-up training services from Beijing Yinglun Yucai Education Consulting Co., Ltd. (“Yinglun Yucai”) which was owned by Mr. Liang Ma. The acquired business is operated by Zhengbao Yucai, an entity established by Beijing Champion. Upon the completion of the acquisition, Beijing Champion transferred 40% equity interest of Zhengbao Yucai to Mr. Liang Ma.

The initial consideration for this acquisition was US\$5,318 in cash, including US\$56 of transaction costs, of which US\$5,314 and US\$4 were paid during the fiscal year 2009 and 2010 respectively.

In addition, the purchase agreement provides for further contingent consideration to be paid or received by Beijing Champion as follows:

- For the fiscal year of 2009, if Zhengbao Yucai has a net income greater than RMB22,500 (approximately US\$3,296), Beijing Champion will pay Mr. Liang Ma an additional cash consideration equal to 40% of the excess amount of net income over RMB22,500.
- For the fiscal year of 2010, if Zhengbao Yucai has a net income greater than RMB47,000 (approximately US\$6,881), Beijing Champion will pay Mr. Liang Ma an additional cash consideration equal to 30% of the excess amount of net income over RMB47,000.
- If Zhengbao Yucai’s net income for the fiscal year of 2009 is less than RMB22,500 or for the fiscal year of 2010 is less than RMB47,000, Mr. Liang Ma will pay Beijing Champion a specified amount of cash which Mr. Liang Ma may settle in stock of Zhengbao Yucai.

The purchase agreement also includes the following call and put options:

- If Zhengbao Yucai has a net loss for the fiscal year of 2009 or 2010, Beijing Champion has the option to sell its equity interest of Zhengbao Yucai back to Mr. Liang Ma for RMB43,200 in cash.
- Beijing Champion has the option to acquire an additional 30% equity interest of Zhengbao Yucai in the next 5 years starting from the end of the fiscal year 2009 at a price equal to 30% of six times of the net income of Zhengbao Yucai for the preceding fiscal year. Zhengbao Yucai has the option to acquire up to 49% equity interest of Beijing Yinhong International Education Consulting Co. Ltd. (“Yinhong”), owned by Yinglun Yucai, within 3 years starting from February 15, 2009 at a price up to 49% of six times of the net income of Yinhong for the preceding fiscal year.

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**3. ACQUISITIONS - continued**

*Acquisition of Zhengbao Yucai - continued*

The following table presents the allocation of the purchase price to the fair values of the portion of the assets acquired and liabilities assumed on March 10, 2009, which were determined by the Group with the assistance of American Appraisal China Limited, an independent valuation firm.

	<u>US\$</u>	<u>Amortization period</u>
Cash	2,854	
Property, plant and equipment	138	
Purchased call options	1,221	
Other intangible assets:		
Business contracts	476	3~5 years
Copyrights	586	5 years
Platform	195	3.5 years
Domain names	168	10~11 years
Software	311	3 years
Courseware	255	5 years
Deferred tax liability	(382)	
Noncontrolling interest	(2,107)	
Goodwill	<u>1,603</u>	
Total consideration	<u><u>5,318</u></u>	

Zhengbao Yucai incurred net losses for the fiscal years of 2009 and 2010. In addition, the Group noted that Mr. Liang Ma, the selling equity holder of Zhengbao Yucai, Yinglun Yucai, a company owned by Mr. Liang Ma, and Global Education Consortium Group Co., Limited, a company owned by Mr. Liang Ma's wife engaged in competing businesses which is prohibited under the purchase agreement.

In January 2010, the Group filed an arbitration application with the China International Economic and Trade Arbitration Commission ("CIETAC"), against Mr. Liang Ma and its related parties ("the respondents") for breach of the original purchase agreement.

As of September 30, 2010, the option to acquire equity interest in Yinhong was fully impaired by US\$34 and the option to acquire equity interest in Zhengbao Yucai was impaired by US\$128 for the year ended September 30, 2010.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 3. ACQUISITIONS - continued

##### *Acquisition of Zhengbao Yucai - continued*

On June 1, 2011, the CIETAC awarded the Group (i) US \$571 compensation from the respondents, which was received on July 27, 2011 and was recorded as other operating income, and (ii) 40% equity interest of Zhengbao Yucai with no consideration from Mr. Liang Ma, which was recorded as equity transaction with no gain or loss recognized. Thereafter, the Group fully impaired the option to acquire equity interest in Zhengbao Yucai by US\$1,115 to nil. (See note 11).

##### *Acquisition of Champion Xinlixiang*

On September 30, 2009, Champion Wangge acquired the Gaokao retake business from Mr. Junnan Ye and Mr. Xiujie Hu, two third-party individuals. The acquired business is operated by Champion Xinlixiang, an entity established by Champion Wangge. Upon the completion of the acquisition, Champion Wangge transferred 40% equity interest of Champion Xinlixiang to Mr. Junnan Ye and Mr. Xiujie Hu.

The initial consideration for this acquisition was US\$2,379 in cash (RMB16,000), including US\$37 of transaction costs, which was fully settled in the fiscal year of 2011.

In addition, the purchase agreement provides for further contingent consideration to be paid or received by Champion Wangge as follows:

- For the fiscal year of 2010, if Champion Xinlixiang has a net income greater than RMB8,000 (approximately US\$1,172), Champion Wangge will pay Mr. Junnan Ye and Mr. Xiujie Hu an additional cash consideration equal to 40% of the excess amount of net income over RMB8,000.
- For the fiscal year of 2011, if Champion Xinlixiang has a net income greater than RMB16,000 (approximately US\$2,344), Champion Wangge will pay Mr. Junnan Ye and Mr. Xiujie Hu an additional cash consideration equal to 30% of the excess amount of net income over RMB16,000.
- If Champion Xinlixiang's net income for the fiscal year of 2010 is less than RMB8,000 or for the fiscal year of 2011 is less than RMB16,000, Mr. Junnan Ye and Mr. Xiujie Hu will pay Champion Wangge a specified amount of cash which Mr. Junnan Ye and Mr. Xiujie Hu may settle in stock of Champion Xinlixiang.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
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**3. ACQUISITIONS - continued**

*Acquisition of Champion Xinlixiang - continued*

The purchase agreement also included the following call and put options:

- If Champion Xinlixiang has a net loss for the fiscal year of 2010 or 2011, Champion Wangge has the option to sell its equity interest of Champion Xinlixiang back to Mr. Junnan Ye and Mr. Xiujie Hu for RMB19,200 in cash.
- Champion Wangge, beginning October 1, 2011, has the option to acquire an additional 40% equity interest of Champion Xinlixiang at a price equal to 40% of six times of the net income of Champion Xinlixiang for the preceding fiscal year. Mr. Junnan Ye and Mr. Xiujie Hu, beginning October 1, 2011, have the right to request Champion Wangge to purchase their equity interest of Champion Xinlixiang at the same price. Upon the refusal of Champion Wangge, the sellers have the right to sell their equity interest of Champion Xinlixiang to a third party at a price no lower than Champion Wangge's purchase price.

The following table presents the allocation of the purchase price to the fair values of the portion of the assets acquired and liabilities assumed on September 30, 2009, which were determined by the Group with the assistance of American Appraisal China Limited, an independent valuation firm.

	<u>US\$</u>	<u>Amortization period</u>
Accounts receivable	1,968	
Purchased call option	669	
Other intangible assets:		
Non-compete agreement	650	15 years
Supplementary domain names	1	10 years
Deferred revenue	(1,617)	
Deferred tax liability	(330)	
Income tax payable	(61)	
Other payables	(107)	
Noncontrolling interest	(937)	
Goodwill	<u>2,143</u>	
Total consideration	<u>2,379</u>	

The purchased call option to acquire additional equity interest in Champion Xinlixiang was recorded at fair value at the acquisition date. Since it is not a derivative because the net settlement criterion is not met, the purchased call option is not subsequently marked to market. As Champion Xinlixiang incurred a net loss in the fiscal year of 2010, pursuant to the terms of the original purchase agreement, the selling equity holders surrendered their 40% equity interest of US\$911 in Champion Xinlixang to the Group for no consideration on October 1, 2010. As a result, the purchase call option was impaired by US\$ 477 and US\$201 in fiscal years of 2010 and 2011, respectively, (see Note 11).

On September 27, 2011, the Group decided to discontinue its Gaokao retake education services business (see note 4).



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**3. ACQUISITIONS - continued**

*Acquisition of Champion Xinlixiang - continued*

No supplemental information on a pro forma basis has been presented for the above acquisitions as such information is not available without unreasonable effort and cost.

**4. DISCONTINUED OPERATIONS**

Gaokao retake business operated by Champion Xinlixiang has been in a loss position. As a result, on September 27, 2011, the Company decided to discontinue operations of Gaokao retake business and put the related assets and business up for sale. The Company has a plan to sell this operation before September 1, 2012. Financial statements for fiscal years of 2009 and 2010 have been adjusted to present the operations of Champion Xinlixiang as a discontinued operation.

In conjunction with the discontinuance of operations, the Company recorded an impairment loss of US\$2,063 in fiscal year 2011 to write down the related carrying amounts of its assets to their fair values less cost to sell. The assets and liabilities of the discontinued operations are presented separately under the captions "Current (Long-term) assets of discontinued operations" and "Current (Non-current) liabilities of discontinued operations," in the accompanying consolidated balance sheets at September 30, 2010 and 2011, respectively and consist of the following:

	<b>As of September 30,</b>	
	<b>2010</b>	<b>2011</b>
	<b>US\$</b>	<b>US\$</b>
<b>Current assets of discontinued operations:</b>		
Cash and cash equivalents	1,450	1,209
Accounts receivable, net	2,905	14
Prepayment and other current assets	271	309
Property, plant and equipment, net	—	774
	<b>4,626</b>	<b>2,306</b>
<b>Long-term assets of discontinued operations:</b>		
Property, plant and equipment, net	722	—
Goodwill	764	—
Other intangible assets, net	343	—
Purchased call option	200	—
	<b>2,029</b>	<b>—</b>
<b>Current liabilities of discontinued operations:</b>		
Accrued expenses and other liabilities	2,839	548
Income tax payable	147	126
Deferred revenue, current portion	1,309	1,186
	<b>4,295</b>	<b>1,860</b>
<b>Non-current liabilities of discontinued operations:</b>		
Deferred tax liabilities-non-current portion	136	—

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**4. DISCONTINUED OPERATIONS - continued**

Summarized operating results from the discontinued operations included in the Group's consolidated statement of operations were as follows for the years ended September 30, 2009, 2010 and 2011:

	<u>Years ended September 30,</u>		
	<u>2009</u>	<u>2010</u>	<u>2011</u>
	US\$	US\$	US\$
Revenues	—	2,167	1,776
Pre-tax profit (loss) from discontinued operations	2	(2,202)	(3,444)
Income tax expense	—	116	144
Income (loss) from discontinued operations, net of tax	2	(2,086)	(3,300)
Net loss of discontinued operations attributable to noncontrolling interest, net of tax	—	33	—
Net (loss) income from discontinued operations attributable to China Distance Education Holding Limited, net of tax	<u>2</u>	<u>(2,053)</u>	<u>(3,300)</u>

All notes to the accompanying consolidated financial statements have been retrospectively adjusted to reflect the effect of the discontinued operations, where applicable.

**5. ACCOUNTS RECEIVABLE, NET**

Accounts receivable, net consisted of the following:

	<u>As of September 30,</u>	
	<u>2010</u>	<u>2011</u>
	US\$	US\$
Accounts receivable	6,248	7,851
Less: allowance for doubtful accounts	<u>(2,236)</u>	<u>(3,190)</u>
Accounts receivable, net	<u>4,012</u>	<u>4,661</u>

The allowance for doubtful accounts as of September 30, 2010 and 2011 were primarily related to accounts receivables of government agencies which have been outstanding for more than a year and are probably uncollectable.

Movement of allowance for doubtful accounts was as follows:

	<u>As of September 30,</u>	
	<u>2010</u>	<u>2011</u>
	US\$	US\$
Balance at beginning of year	—	2,236
Charged to expenses	2,197	824
Foreign currency adjustment	<u>39</u>	<u>130</u>
Balance at end of the year	<u>2,236</u>	<u>3,190</u>

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**6. INVENTORIES, NET**

Inventories consisted of the following:

	As of September 30,	
	2010	2011
	US\$	US\$
Finished goods	416	285
Raw materials	183	78
	599	363

Inventories provision as of September 30, 2009, 2010 and 2011 were US\$3, US\$2 and US\$3, respectively.

**7. PREPAYMENT AND OTHER CURRENT ASSETS**

Prepayment and other current assets consisted of the following:

	Notes	As of September 30,	
		2010	2011
		US\$	US\$
Advance to the suppliers	(1)	143	1,585
Prepaid expenses		668	618
Refundable prepayments	(2)	306	320
Funds receivable	(3)	307	245
Prepaid course remuneration		119	—
Deposits		59	56
Others		437	357
Less: allowance for doubtful accounts	(2)	—	(320)
Prepayment and other current assets, net		2,039	2,861

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 7. PREPAYMENT AND OTHER CURRENT ASSETS - continued

- (1) Advance to the suppliers represents interest-free cash deposits paid to suppliers for future purchase of raw materials and finished goods. The risk of loss arising from non-performance by or bankruptcy of the suppliers is assessed prior to making the deposits and is monitored on a regular basis by management. A charge to cost of sales will be recorded in the period in which a loss is incurred. To date, the Group has not experienced any loss of advances to suppliers.
- (2) The group prepaid a refundable fee to a government agency in 2010 as a sponsor of ITAT contest which was subsequently cancelled. In 2011, the Group recorded a full allowance as such prepaid amount has been outstanding for more than a year and is probably uncollectable.
- (3) Funds receivable arise due to the time taken to clear customers' payment transactions through external payment networks. When customers remit fees to the Group via external payment networks using their bank account or credit card, there is a clearing period before the cash is received by the Group which usually takes one to three business days. These fees are treated as a receivable until the cash is received.

#### 8. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment consisted of the following:

	As of September 30,	
	2010	2011
	US\$	US\$
Buildings	4,840	5,077
Electronic and office equipment	5,065	6,020
Leasehold improvement and building improvement	1,034	917
Motor vehicles	573	1,293
Total	11,512	13,307
Less: Accumulated depreciation	(3,430)	(4,721)
	<u>8,082</u>	<u>8,586</u>

Depreciation expenses from continuing operations were US\$930, US\$1,142 and US\$1,309, and from discontinued operations were nil, US\$15 and US\$140, for the years ended September 30, 2009, 2010 and 2011, respectively.

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**9. GOODWILL**

Goodwill was comprised of the following:

	<u>Online education service</u> US\$	<u>Start-up training service</u> US\$	<u>Total</u> US\$
<u>Gross amount</u>			
Balance as of September 30, 2009	5,272	1,614	6,886
Foreign currency adjustment	105	33	138
Balance as of September 30, 2010	5,377	1,647	7,024
Foreign currency adjustment	265	114	379
Balance as of September 30, 2011	<u>5,642</u>	<u>1,761</u>	<u>7,403</u>

The Group tested its goodwill for impairment at the following reporting units level.

Online education service - This reporting unit provides online education services to its customers located in the PRC. It includes all the subsidiaries, the VIE and VIE's subsidiaries of the Group except for Zhengbao Yucai and Champion Xinlixiang. The goodwill arising from the acquisitions of the entities under this reporting unit is fully allocated to this reporting unit.

Start-up training service - This reporting unit provides start-up training services to the Group's customers located the PRC. It includes Zhengbao Yucai. The goodwill arising from the acquisitions of 60% equity interest in Zhengbao Yucai is fully allocated to this reporting unit.

Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate that it might be impaired. The Group has not recorded any impairment of goodwill on online education service and start-up training service.

The reporting unit of Gaokao retake business was discontinued and accordingly the related goodwill was fully impaired at the end of fiscal year 2011. (See note 4).

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**10. OTHER INTANGIBLE ASSETS, NET**

Other intangible assets consisted of the following:

	<u>As of September 30,</u>	
	<u>2010</u>	<u>2011</u>
	US\$	US\$
Computer software	1,803	2,278
Trademarks and domain names	1,251	1,337
Website	97	102
Courseware	446	468
Business contracts	486	510
Copyrights	597	627
Platform	199	208
Total intangible assets	4,879	5,530
Less: Accumulated amortization		
Computer software	(887)	(1,369)
Trademarks and domain names	(443)	(585)
Website	(80)	(92)
Courseware	(266)	(334)
Business contracts	(172)	(296)
Copyrights	(186)	(320)
Platform	(88)	(152)
Accumulated amortization	<u>(2,122)</u>	<u>(3,148)</u>
Intangible assets, net	<u>2,757</u>	<u>2,382</u>

Amortization expenses from continuing operations were US\$579, US\$809 and US\$900, and from discontinued operations were nil, US\$42 and US\$26, for the years ended September 30, 2009, 2010 and 2011, respectively.

The estimated amortization expenses for the above other intangible assets for each of the following fiscal years are as follows

	<u>Amortization</u>
	US\$
2012	834
2013	652
2014	375
2015	219
2016	143
2017 and thereafter	159
	<u>2,382</u>

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**10. OTHER INTANGIBLE ASSETS, NET - continued**

The intangibles related to non-compete agreement of Gaokao retake business has been fully impaired due to the discontinuance of Gaokao retake business. (See note 11).

**11. FAIR VALUE MEASUREMENT**

The Group's financial instruments consist of cash equivalents, term deposits, restricted cash, accounts receivable, other current assets, and other liabilities. The carrying amounts of these instruments approximate their fair values due to their short-term maturity.

The Group reviews goodwill for impairment annually or more frequently if events or changes in circumstances indicate the possibility of impairment. For the continuing operations, other intangible assets, purchased call options and other long-lived assets are measured at fair value on a nonrecurring basis when there is an indicator of impairment, and they are recorded at fair value only when impairment is recognized. For discontinued operations, such long-lived assets are measured at the lower of carrying amount or fair value less cost to sell.

These assets, as presented below are considered Level 3 assets because the Group used unobservable inputs, reflecting the Group's assessment of the assumptions market participants would use in valuing these assets.

<u>Zhengbao Yucai</u>	<u>Purchased call options (acquisition of 30% interest in Zhengbao Yucai)</u> US\$
Balance as of September 30, 2009	1,222
Impairment during the year	(162)
Foreign currency adjustment	23
Balance as of September 30, 2010	1,083
Impairment during the year	(1,115)
Foreign currency adjustment	32
Balance as of September 30, 2011	—

Based on an impairment test performed as of September 30, 2010, the purchased call options to acquire 40% equity interest in Zhengbao Yucai were impaired by US\$162. As of September 30, 2011, the purchased call options acquired with the acquisitions of Zhengbao Yucai were written down to zero, because the Group acquired the additional 40% equity interest of Zhengbao Yucai in 2011 with no consideration. (See note 3)

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**11. FAIR VALUE MEASUREMENT - continued**

<u>Champion Xinlixiang-Gaokao Retake business</u>	<u>Goodwill</u> US\$	<u>Property plant and equipment</u> US\$	<u>Non-compet agreement</u> US\$	<u>Purchased call options (acquisition of 40% interest in Champion Xinlixiang)</u> US\$
Balance as of September 30, 2009	2,144	—	651	670
Addition during the year	—	725	—	—
Amortization during the year	—	(17)	(34)	—
Impairment during the year	(1,407) (1)	—	(274) (2)	(477) (4)
Foreign currency adjustment	27	14	—	7
Balance as of September 30, 2010	764	722	343	200
Addition during the year	—	1,110	—	—
Amortization during the year	—	(140)	(25)	—
Impairment during the year	(758) (1)	(973) (3)	(332) (3)	(201) (4)
Foreign currency adjustment	(6)	55	13	1
Balance as of September 30, 2010	<u>—</u>	<u>774</u>	<u>—</u>	<u>—</u>

- (1) The Group used the discounted cash flow (“DCF”) method of the income approach to assess the fair value of each reporting unit. The discounted cash flow for each reporting unit was projected based on financial forecast developed by management for planning purposes. Cash flows beyond the forecast periods were estimated using a terminal value calculation, which incorporated historical and forecasted financial trends for each reporting unit. Publicly available information regarding the market capitalization of the Group was also considered in assessing the reasonableness of the aggregate fair value of all the reporting units estimated using the income approach valuation methodology. Based on the goodwill impairment test as of September 30, 2010 and 2011, an impairment loss of US\$1,407 and US\$758 was recorded for Gaokao retake business.
- (2) Measured at lower of carrying amount or fair value, the non-compet agreement was impaired by US\$274 during the year ended September 30, 2010.
- (3) Measured at the lower of carrying amount or fair value less cost to sell, the property plant, equipment and non-compet agreement were impaired by US\$973 and US\$332 during the year ended September 30, 2011, respectively.
- (4) The purchased call options acquired with the acquisitions of Champion Xinlixiang were re-measured using binomial model at September 30, 2010, and the option to purchase additional equity interest in Champion Xinlixiang was impaired by US\$477. As of September 30, 2011, such purchased call option was fully impaired because the Group acquired the 40% equity interest for no consideration on October 1, 2010. (See Note 3)



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**12. DEPOSITS FOR NON-CURRENT ASSETS**

Deposits for non-current assets consisted of the following:

	As of September 30,	
	2010	2011
	US\$	US\$
Deposit for purchase of property, plant and equipment	—	242
	—	242
	—	242

**13. OTHER NON-CURRENT ASSETS**

Other non-current assets consisted of the following:

	As of September 30,	
	2010	2011
	US\$	US\$
Long-term prepaid expenses	624	129
Rental deposits	108	587
Others	12	13
	744	729
	744	729

Long-term prepaid expenses represent prepaid service fee for obtaining government authorization to provide the ITAT program, an information technique application training program, for a period of ten years. The amortization of the long term prepaid expenses was included in “cost of sales” on the consolidated statements of operations.

Rental deposits represent office rental deposits for the Group’s daily operations. These deposits are classified as non-current deposits since they will not be refunded within one year.

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**14. ACCRUED EXPENSES AND OTHER LIABILITIES**

The components of accrued expenses and other liabilities are as follows:

	<u>As of September 30,</u>	
	<u>2010</u>	<u>2011</u>
	<u>US\$</u>	<u>US\$</u>
Accrued expenses	1,786	2,172
Salary and welfare payable	1,199	1,414
Other payable	380	1,235
Remuneration payable to lecturers	295	1,523
Uncertain income tax liabilities (Note 18)	162	170
	<u>3,822</u>	<u>6,514</u>

Other payable mainly represents other tax liabilities including business tax payable, value-added tax payable and withholding individual income tax payable.

**15. ORDINARY SHARES**

All share and per share data before January 11, 2008, the inception date of the Company, are presented to give retroactive effect to the share exchange between CDEL Hong Kong and the Company at a ratio of 1,000 shares in the Company to 1 share in CDEL Hong Kong.

On August 4, 2008, the Company completed its initial public offering of 35,000,000 ordinary shares. Immediately prior to the initial public offering, 12,996,000 Series A Shares were converted into 14,963,594 ordinary shares.

On November 20, 2008, the Company's board of directors approved a share repurchase program effective November 20, 2008. Under the approved program, the Company is authorized to repurchase up to US\$10 million worth of its issued and outstanding ADSs from time to time in open-market transactions on NYSE. On April 29, 2011, the Company's board of directors approved additional share repurchase up to US\$10 million worth of its issued and outstanding ADSs. During the years ended September 30, 2010 and 2011, the Company repurchased 1,909,600 and 9,223,188 ordinary shares for total considerations of US\$2,172 and US\$8,138, respectively. Such shares were immediately canceled after the repurchase.

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### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 16. RESTRICTED NET ASSETS

Relevant PRC statutory laws and regulations permit payments of dividends by the Group's PRC subsidiaries only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. The results of operations reflected in the financial statements prepared in accordance with U.S. GAAP differ from those reflected in the statutory financial statements of the Company's subsidiaries.

In accordance with the Regulations on Enterprises with Foreign Investment of China and their articles of association, a foreign invested enterprise established in the PRC is required to provide certain statutory reserves, namely general reserve fund, the enterprise expansion fund and staff welfare and bonus fund which are appropriated from net profit as reported in the enterprise's PRC statutory accounts, which is presented at cumulative deficits accounts in equity section of balance sheet. A wholly-owned foreign invested enterprise is required to allocate at least 10% of its annual after-tax profit to the general reserve until such reserve has reached 50% of its respective registered capital based on the enterprise's PRC statutory accounts. Appropriations to the enterprise expansion fund and staff welfare and bonus fund are at the discretion of the board of directors for all foreign invested enterprises. The aforementioned reserves can only be used for specific purposes and are not distributable as cash dividends. Champion Technology and Champion Education Technology were established as wholly-owned foreign invested enterprises and therefore are subject to the above mandated restrictions on distributable profits.

Additionally, in accordance with the Company Law of the PRC, a domestic enterprise is required to provide statutory common reserve at least 10% of its annual after-tax profit until such reserve has reached 50% of its respective registered capital based on the enterprise's PRC statutory accounts. A domestic enterprise is also required to provide for discretionary surplus reserve, at the discretion of the board of directors, from the profits determined in accordance with the enterprise's PRC statutory accounts. The aforementioned reserves can only be used for specific purposes and are not distributable as cash dividends. Beijing Champion was established as a domestic invested enterprise and therefore is subject to the above mandated restrictions on distributable profits.

As a result of these PRC laws and regulations, appropriation to the statutory reserve amounted to US\$1,053, US\$1,076 and US\$2,388 for the years ended September 30, 2009, 2010 and 2011, respectively. As of September 30, 2011, the aggregate amount of net assets of the relevant subsidiaries, VIE and VIE's subsidiaries in the Group not available for distribution was US\$15,612.

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**17. NONCONTROLLING INTERESTS**

Effective October 1, 2009, the Group adopted authoritative guidance regarding noncontrolling interests, which clarifies that a noncontrolling interests in a subsidiary is an ownership interest in the consolidated entity and should be reported as equity on the financial statements. The authoritative guidance requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interests. Furthermore, disclosure of the amounts of consolidated net income attributable to the parent and to the noncontrolling interests is required on the face of the financial statements.

On March 10, 2009, Beijing Champion acquired 60% of the equity interest in start-up training services. On September 30, 2009, Champion Wangge acquired 60% of the equity interest in Gaokao retake business. The Group's noncontrolling interests represented 40% of the equity interest in start-up training service (Zhengbao Yucai) and Gaokao retake business (Champion Xinlixiang), respectively.

On June 1, 2011, the Group obtained 40% equity interest of Zhengbao Yucai through arbitration with no consideration, which was accounted for as equity transaction with no gain or loss recognized. (See note 3)

On October 1, 2010, as Champion Xinlixiang incurred a net loss in year 2010, pursuant to the terms of the original purchase agreement, the selling equity holders transferred their 40% equity interest in Champion Xinlixiang to the Group for no consideration. The acquisition was accounted for as equity transaction with no gain or loss recognized. (See note 3).

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**17. NONCONTROLLING INTERESTS - continued**

	<u>Start-up training business</u> US\$	<u>Gaokao retake business</u> US\$	<u>Total</u> US\$
Balance as of September, 30, 2008	—	—	—
Noncontrolling interest arising from acquisition of start-up training business	2,110	—	2,110
Noncontrolling interest arising from acquisition of Gaokao retake business	—	937	937
Net loss for the year	(82)	—	(82)
Foreign currency translation adjustments	(2)	—	(2)
Balance as of September 30, 2009	<u>2,026</u>	<u>937</u>	<u>2,963</u>
Net loss for the year	(911)	(33)	(944)
Foreign currency translation adjustments	11	7	18
Balance as of September 30, 2010	<u>1,126</u>	<u>911</u>	<u>2,037</u>
Net loss for the year	(303)	—	(303)
Foreign currency translation adjustments	33	—	33
Acquisition of noncontrolling interest of start-up training business	(856)	—	(856)
Acquisition of noncontrolling interest of Gaokao retake business	—	(911)	(911)
Balance as of September 30, 2011	<u>—</u>	<u>—</u>	<u>—</u>

**18. TAXATION**

*Cayman Islands*

Under current law of Cayman Islands, the Company is not subject to income or capital gains taxes. In addition, dividends payments are not subject to tax withholding in the Cayman Islands.

*Hong Kong*

CDEL Hong Kong and PENCIL have not recorded tax provision for Hong Kong profits tax as the companies have not had assessable profits arising in or derived from Hong Kong.

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**18. TAXATION - continued**

*China*

The Enterprise Income Tax Law (the “EIT Law”) of the PRC, which took effect on January 1, 2008, has applied a uniform 25% enterprise income tax rate to all resident enterprise in China, including foreign invested enterprises.

In 2008, Beijing Champion and Champion Technology qualified as “high and new technology enterprise strongly supported by the State” (“HNTE”) under the EIT Law, and therefore, were entitled to preferential income tax rates. Beijing Champion is subject to the tax rate of 15% from 2008 through 2010. Champion Technology is subject to the tax rate of 7.5% for 2008 through 2009 and 15% for 2010.

The HNTE status is valid for three years and qualifying entities can then apply to renew for an additional three years provided that the company’s business operations continue to qualify for HNTE status. In October 2011, Beijing Champion and Champion Technology renewed the HNTE qualification, and therefore, were continually entitled to the preferential income tax rate of 15% in years 2011 through 2013.

In general, the PRC tax authorities have up to five years to conduct examinations of the PRC entities’ tax filings. Accordingly, the PRC entities’ tax years from 2006 to 2010 remain subject to examination by the tax authorities.

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**18. TAXATION - continued**

*China - continued*

Income (loss) before income taxes from continuing operations consisted of:

	Years ended September 30,		
	2009	2010	2011
	US\$	US\$	US\$
Non - PRC	(4,668)	(5,030)	(6,873)
PRC	7,250	4,849	7,039
	2,582	(181)	166

The current and deferred components of the income tax benefit/(expense) from continuing operations appearing in the consolidated statements of operations are as follows:

	Years ended September 30,		
	2009	2010	2011
	US\$	US\$	US\$
Current tax expense	148	1,044	1,948
Deferred tax (benefit)/expense	1,330	(469)	(977)
	1,478	575	971

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**18. TAXATION - continued**

*China - continued*

The reconciliation of the effective tax rate and the statutory income tax rate applicable to PRC operations is as follows:

	Years ended September 30,		
	2009 US\$	2010 US\$	2011 US\$
(Loss)/Income before taxes	2,582	(181)	166
Income tax expense/(benefit) computed at applicable tax rates of 25%	646	(45)	42
Effect of different tax rates in different jurisdictions	1,107	1,224	1,667
Non-deductible expenses	177	223	260
Effect of tax holidays	(988)	(936)	(860)
Effect of tax rate changes	500	—	—
Effect of valuation allowances	132	109	(138)
Decrease in unrecognized tax benefit balance	(96)	—	—
	<u>1,478</u>	<u>575</u>	<u>971</u>
Effective income tax rate	<u>57.24%</u>	<u>(317.68%)</u>	<u>584.94%</u>

The authoritative guidance requires that the Group recognizes the impact of a tax position in the financial statements if that position is more likely than not of being sustained upon audit by the tax authority, based on the technical merits of the position. Under PRC laws and regulations, arrangements and transactions among related parties may be subject to examination by the PRC tax authorities. If the PRC tax authorities determine that the contractual arrangements among related companies do not represent a price under normal commercial terms, they may make adjustments to the companies' income and expenses. A transfer pricing adjustment could result in additional tax liabilities.

As a result of the Group's assessment of its tax positions, the unrecognized tax benefit was recorded US\$159, US\$ 163 and US\$ 170 as of September 30, 2009, 2010 and 2011, respectively. The subsequent changes of the unrecognized tax benefit were due to foreign currency adjustment.



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**18. TAXATION - continued**

*China - continued*

Reconciliation of accrued unrecognized tax benefits is as follows:

	<b>Unrecognized tax benefits</b>
Balance - September 30, 2009	159
Foreign currency adjustment	3
Balance - September 30, 2010	162
Foreign currency adjustment	8
Balance - September 30, 2011	170

The unrecognized tax benefits would impact the effective tax rate, if recognized in connection with the normal tax return preparation. It is possible that the amount of unrecognized tax benefits will change in the next twelve months. However, an estimate of the range of the possible change cannot be made at this time.

The aggregate amount and per share effect of the tax holidays are as follows:

	<b>Years ended September 30,</b>		
	<b>2009</b>	<b>2010</b>	<b>2011</b>
	<b>US\$</b>	<b>US\$</b>	<b>US\$</b>
The aggregate amount of tax holidays	988	936	860
The aggregate effect on basic and diluted net income per share:			
- Basic	0.01	0.01	0.01
- Diluted	0.01	0.01	0.01

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**18. TAXATION - continued**

*China - continued*

Deferred taxes reflect the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The components of deferred taxes from continuing operations are as follows:

	<u>As of September 30,</u>	
	<u>2010</u>	<u>2011</u>
	US\$	US\$
<b>Current deferred tax assets</b>		
Payroll payable	176	217
Accrued expenses	185	439
Allowance for doubtful accounts	523	822
Net operating loss carry-forwards	133	78
<b>Total current deferred tax assets</b>	<u>1,017</u>	<u>1,556</u>
Less: valuation allowance	(1)	—
<b>Current deferred tax assets, net</b>	<u>1,016</u>	<u>1,556</u>
<b>Non-current deferred tax assets</b>		
Intangible assets	147	116
Property, plant and equipment	143	147
Net operating loss carry-forwards	628	670
<b>Total non-current deferred tax assets</b>	<u>918</u>	<u>933</u>
Less: valuation allowance	(236)	(66)
<b>Non-current deferred tax assets, net</b>	<u>682</u>	<u>867</u>
<b>Non-current deferred tax liabilities</b>		
Intangible assets	258	199
Purchased call option	271	—
<b>Total non-current deferred tax liabilities</b>	<u>529</u>	<u>199</u>

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 18. TAXATION - continued

##### *China - continued*

Uncertainties exist with respect to how the current income tax law in the PRC applies to the Group's overall operations, and more specifically, with regard to tax residency status. The New EIT Law includes a provision specifying that legal entities organized outside of the PRC will be considered residents for Chinese Income tax purposes if the place of effective management or control is within the PRC. The implementation rules to the New EIT Law provide that non-resident legal entities will be considered PRC residents if substantial and overall management and control over the manufacturing and business operations, personnel, accounting and properties, occurs within the PRC. Despite the present uncertainties resulting from the limited PRC tax guidance on the issue, the Group does not believe that the legal entities organized outside of the PRC within the Group should be treated as residents for EIT law purposes. If the PRC tax authorities subsequently determine that the Company and its subsidiaries registered outside the PRC should be deemed resident enterprises, the Company and its subsidiaries registered outside the PRC will be subject to the PRC income taxes, at a rate of 25%.

If any entity within the Group that is outside the PRC were to be a non-resident for PRC tax purposes dividends paid to it out of profits earned after January 1, 2008 would be subject to a withholding tax at a rate of 10%, subject to reduction by an applicable tax treaty with the PRC.

Aggregate undistributed earnings of the Company's subsidiaries located in the PRC that are available for distribution at September 30, 2011 are considered to be indefinitely reinvested and accordingly, no provision has been made for the Chinese dividend withholding taxes that would be payable upon the distribution of those amounts to any entity within the Group that is outside the PRC.

The Group does not have any present plan to pay any cash dividends on its ordinary shares in the foreseeable future. It intends to retain most of its available funds and any future earnings for use in the operation and expansion of its business. As of September 30, 2011, the Group has not declared any dividends.

#### 19. EMPLOYEE DEFINED CONTRIBUTION PLAN

Full time employees of the Group in the PRC participate in a government mandated defined contribution plan, pursuant to which certain pension benefits, medical care, employee housing fund and other welfare benefits are provided to employees. Chinese labor regulations require that the PRC subsidiaries of the Group make contributions to the government for these benefits based on certain percentages of the employees' salaries. The Group has no legal obligation for the benefits beyond the contributions made. The total amounts for such employee benefits, which were expensed as incurred, were US\$1,350, US\$1,915 and US\$2,464 for the years ended September 30, 2009, 2010 and 2011, respectively. Employee benefits from continuing operations were US\$1,350, US\$1,842 and US\$2,412, and from discontinued operations were nil, US\$73 and US\$52 for the years ended September 30, 2009, 2010 and 2011, respectively.

Obligations for contributions to defined contribution retirement plans for full-time employee in Hong Kong, including contributions payable under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognized as expenses in the income statement as incurred. The total amounts for such employee benefits were US\$2, US\$2 and US\$2 for the years ended September 30, 2009, 2010 and 2011, respectively.

CHINA DISTANCE EDUCATION HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)

20. COMMITMENTS AND CONTINGENCIES

*Operating lease commitments*

Future minimum payments under non-cancelable operating leases related to offices, servers and bandwidth with initial terms of one-year or more consisted of the following at September 30, 2011:

Years ending September 30,	US\$
2012	2,941
2013	2,105
2014	204
	<u>5,250</u>

Payments under operating leases are expensed on the straight-line basis over the periods of their respective leases. The terms of the leases do not contain rent escalation or contingent rents. For the years ended September 30, 2009, 2010 and 2011, total rental expenses from continuing operations for all operating leases amounted to US\$1,555, US\$2,686 and US\$2,844, respectively. Rental expenses from discontinued operations for all operating leases amounted to nil, US\$789 and US\$750, respectively.

*Legal contingencies*

The group is a party in potential claims arising in the ordinary course of business. The Group does not believe that the resolution of these matters will have a material adverse effect on its financial position or results of operations.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 21. SEGMENT REPORTING

The Group operates and manages its business as a single segment that includes primarily the provision of online and offline education services and selling of related products.

The revenues attributable to the different service and product groups are as follows:

	Years ended September 30,		
	2009 US\$	2010 US\$	2011 US\$
Online education services	22,279	23,982	30,788
Books and reference materials	2,709	3,939	4,743
Offline education services	2,576	1,557	2,907
Others	2,557	3,101	3,126
	<u>30,121</u>	<u>32,579</u>	<u>41,564</u>

Online education services accounted for 74.1%, 73.6% and 74.0% of the Group's total net revenue for the years ended September 30, 2009, 2010 and 2011, respectively. Any significant reduction in sales from this service could have a substantial negative impact on the Group's results of operations.

Geographic disclosures:

As the Group primarily generates its revenues from customers in the PRC, no geographical segments are presented. All of the Group's long-lived assets are located in the PRC.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
(In thousands, except share and per share data)

**22. NET (LOSS) INCOME PER SHARE**

Basic and diluted net (loss) income per share for each of the periods presented were calculated as follows:

	Years ended September 30,		
	2009 US\$	2010 US\$	2011 US\$
<b>Numerator:</b>			
Income (loss) from continuing operations	1,186	155	(502)
Income (loss) from discontinued operations, net of tax	2	(2,053)	(3,300)
Net (loss) income	1,188	(1,898)	(3,802)
- allocated to ordinary Share - basic	1,188	(1,898)	(3,800)
-allocated to nonvested restricted share - basic	—	—	(2)
<b>Denominator:</b>			
Weighted average number of ordinary shares outstanding	140,260,811	138,232,493	133,489,261
Weighted average number of nonvested restricted share	—	—	82,466
Plus incremental weighted average ordinary shares from assumed exercise of share options using the treasury stock method	215,130	—	—
Weighted average ordinary shares outstanding used in computing diluted net income per share	<u>140,475,941</u>	<u>138,232,493</u>	<u>133,571,727</u>
<b>Basic net (loss) income per share</b>			
Basic from continuing operations	0.01	—	—
Basic from discontinued operations (net of tax)	—	(0.01)	(0.03)
Basic	<u>0.01</u>	<u>(0.01)</u>	<u>(0.03)</u>
<b>Basic net (loss) income per nonvested restricted share</b>			
Basic from continuing operations	—	—	—
Basic from discontinued operations (net of tax)	—	—	(0.03)
Basic	<u>—</u>	<u>—</u>	<u>(0.03)</u>
<b>Diluted net (loss) income per share</b>			
Diluted from continuing operations	0.01	—	—
Diluted from discontinued operations (net of tax)	—	(0.01)	(0.03)
Diluted	<u>0.01</u>	<u>(0.01)</u>	<u>(0.03)</u>
<b>Basic net (loss) income per share</b>			
- allocated to ordinary Share - basic	0.01	(0.01)	(0.03)
-allocated to nonvested restricted share - basic	—	—	(0.03)
Diluted	0.01	(0.01)	(0.03)

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 23. SHARE INCENTIVE PLAN

##### *Share options*

On April 18, 2008, the Company's shareholders approved the "China Distance Education Holdings Limited Share Incentive Plan" (the "Prior Plan"), which permits the grant of share options and shares to its employees and non-employees (the "Participants"). The maximum number of ordinary shares that may be delivered pursuant to compensatory awards granted to the "Participants" under the Prior Plan should not exceed 11,652,556 ordinary shares of par value US\$0.0001 per share. On July 2, 2008, the Company's shareholders approved the "China Distance Education Holdings Limited 2008 Performance Incentive Plan" (the "New Plan"). Subject to any amendment of the New Plan, the maximum number of ordinary shares that may be issued pursuant to the New Plan is equal to 5% of the total number of ordinary shares issued and outstanding as of August 4, 2008, plus an automatic annual increase on October 1 of each calendar year commencing with October 1, 2008, by an amount equal to the lesser of (i) 1% of the total number of ordinary shares issued and outstanding on September 30 of the same calendar year, or (ii) such number of ordinary shares as may be determined by the Company's board of directors. The purpose of these share incentive plans is to promote the success of the Company and the interests of its shareholders by providing a means through which the Company may grant equity-based incentives to attract, motivate, retain and reward certain officers, employees, directors and other eligible persons and to further link the interests of recipients with those of the Company's shareholders generally. The Prior Plan will expire on April 17, 2018. The New Plan will expire on the tenth anniversary date of August 4, 2008. Option awards are generally granted with an exercise price equal to the market price of the Company's stock at the date of grant; those option awards generally vest within 4 years of continuous service and have 10-year contractual terms. Share awards generally vest for 1 year.

By a resolution of the board of directors on April 18, 2008, 11,652,556 share options were authorized to be granted to certain employees and non-employees. An aggregate of 11,045,500 share options were granted, including a total of 10,060,600 granted to employees on April 18, 2008 and May 31, 2008, and 984,900 granted to non-employees on April 18, 2008 (collectively "the first round"). The share options had an exercise price of US\$2.995966 per share and a graded vesting term of four years. For the options granted to non-employees, the Group determined the measurement date to be the performance commitment date pursuant to the service supplemental agreements, in which the penalty for nonperformance was stipulated and represented a sufficiently large disincentive for nonperformance.

The options would vest as to 25% of the total number of ordinary shares subject to the options on the first anniversary of the vesting commencement date. The remaining 75% of the total number of ordinary shares subject to the options would vest in six substantially equal semi-annual installments, with the first installment vesting on the last day of the sixth month following the month in which the first anniversary of the vesting commencement date occurs and an additional installment vesting on the last day of every six months thereafter.

On November 17, 2008, the Company's board of directors and compensation committee approved to provide a compensation package for the non-executive directors. 400,000 options were granted to five directors on December 2, 2008. These options are subject to a two-year vesting schedule with 50% vesting in each year. The exercise price is US\$0.82 per share which was determined by the closing price of the Company's ADSs on NYSE on December 2, 2008.

## CHINA DISTANCE EDUCATION HOLDINGS LIMITED

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011 (In thousands, except share and per share data)

#### 23. SHARE INCENTIVE PLAN - continued

##### *Share options - continued*

On December 2, 2008 (the “repricing date”), the Company’s board of directors and compensation committee approved to amend the terms of certain stock options granted to 260 employees and 17 non-employees to reduce the exercise price of all outstanding share options from US\$2.995966 per share to US\$0.82 per share based on the closing price of the Company’s ADSs on NYSE on December 2, 2008. The amendments did not change the vesting provisions or the number of shares subject to any of the option awards. This was accounted for as a share option modification and required the remeasurement of the fair value of these share options. This remeasurement resulted in a total incremental share-based compensation of US\$2,699, of which US\$752 and US\$853 were recognized in the year ended September 30, 2009 and 2010, and the remaining is recognized ratably over the remaining vesting period of the award.

By a resolution of the board of directors on November 17, 2009, 1,361,900 share options were granted to selected employees for an exercise price per share equal to US\$1.87. The option shall vest as to 25% of the total number of ordinary shares subject to the option on the first anniversary of the vesting commencement date. The remaining 75% of the total number of ordinary shares subject to the option shall vest in six substantially equal semi-annual installments, with the first installment vesting on the last day of the sixth month following the month in which the first anniversary of the vesting commencement date occurs and an additional installment vesting on the last day of every six months thereafter.

By a resolution of the board of directors on September 27, 2011, 1,000,600 share options were granted to selected employees with an exercise price per share equal to US\$0.615, which was determined by the closing price of the Company’s ADSs on NYSE on September 27, 2011. These options are subject to a two-year vesting schedule with 25% vesting semi-annually. By the same resolution of the board of directors on September 27, 2011, 400,000 fully-vested options were granted to selected directors with an exercise price per share equal to US\$0.615, which was determined by the closing price of the Company’s ADSs on NYSE on September 27, 2011.

Also by that resolution of the board of directors on September 27, 2011, the Company’s board of directors approved to amend the terms of certain stock options granted to 172 employees and 17 non-employees representing 9,465,000 share options. The amendments included (i) reduction of the exercise price of share options from US\$0.82 per share to nil for one selected employee, and to reduce the exercise price of share options from US\$0.82 per share to US\$0.615 per share based on the closing price of the Company’s ADSs on NYSE on September 27, 2011 for the other 171 employees and 17 non-employees; (ii) acceleration of the vesting of share options to fully vested on September 27, 2011; (iii) an option of a three-year interest-free loan for exercising such options. The amendments did not change the vesting provisions or the number of shares subject to any of the option awards. This amendment was accounted for as a share option modification and required the re-measurement of the fair value of these share options. This re-measurement resulted in a total incremental share-based compensation of US\$1,658, all of which was recognized in the year ended September 30, 2011.



**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
(In thousands, except share and per share data)

**23. SHARE INCENTIVE PLAN - continued**

*Share options - continued*

<u>Share option granted to employees and non-executive directors</u>	<u>Number of shares</u>	<u>Weighted-average exercise price</u>	<u>Weighted-average remaining contractual term (years)</u>	<u>Aggregated intrinsic value</u>
Outstanding, October 1, 2010	10,642,892	US\$ 0.92	7.73	3,438
Granted	9,888,388	US\$ 0.53		
Exercised	(91,012)	US\$ 0.82		
Forfeited	(641,608)	US\$ 0.88		
Cancelled	(8,487,788)	US\$ 0.82		
Outstanding, September 30, 2011	<u>11,310,872</u>	US\$ 0.65	7.14	—
Expected to vest, September 30, 2011	<u>1,639,652</u>	US\$ 1.10	9.27	—
Exercisable at September 30, 2011	<u>9,671,220</u>	US\$ 0.58	6.78	645

The weighted-average grant-date fair value of options granted to employees and non-executive directors during the year 2009, 2010 and 2011 was US\$1.40, US\$0.87 and US\$0.26, respectively.

<u>Share option granted to non-employees</u>	<u>Number of shares</u>	<u>Weighted-average exercise price</u>	<u>Weighted-average remaining contractual term (years)</u>	<u>Aggregated intrinsic value</u>
Outstanding, October 1, 2010	977,212	US\$ 0.82	7.55	418
Granted	977,212	US\$ 0.62		
Cancelled	(977,212)	US\$ 0.82		
Outstanding, September 30, 2011	<u>977,212</u>	US\$ 0.62	6.55	27
Exercisable at September 30, 2011	<u>977,212</u>	US\$ 0.62	6.55	27

The weighted-average grant-date fair value of options granted to non-employees during the year 2009, 2010 and 2011 was US\$0.82, nil and US\$0.26 respectively.

The total intrinsic value of options exercised during the year ended September 30, 2011 was US\$30. As of September 30, 2011, the unrecognized share-based compensation cost related to share options amounted to approximately US\$682. This compensation cost is expected to be recognized over a weighted-average vesting period of 2.07 years. Forfeitures were estimated based on historical experience. To the extent the actual forfeiture rate is different from the original estimate, actual share-based compensation expenses related to these awards may be different from the expectation.

CHINA DISTANCE EDUCATION HOLDINGS LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued  
FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011  
(In thousands, except share and per share data)

23. SHARE INCENTIVE PLAN - continued

*Share options - continued*

The fair value of each option award to employees and non-employees was estimated using the Black-Scholes Option Pricing Model by the management of the Company. The volatility assumption was estimated based on the price volatility of the shares of comparable companies in the education business because the Company did not have sufficient data to calculate expected volatility of the price of the underlying ordinary shares over the expected term of the option. The expected term was estimated based on the vesting terms, contractual terms and management's expectation of exercise behavior of the option grantees. The risk-free rate was based on the market yield of China Sovereign Bonds denominated in US\$ with maturity terms equal to the expected term of the option awards. The closing market price of the ordinary shares of the Company as of the grant date was used as the fair value of the ordinary shares on that date.

The Company used the Black Scholes Model to estimate the fair value of the share options on the grant dates with the following assumptions:

	For the year ended September 30,	
	2010	2011
Risk-free interest rate	3.31%	1.40% ~ 1.86%
Dividend yield	—	—
Expected volatility	47%	51%
Expected life (in years)	5.47	3.71 ~ 5.63

*Nonvested restricted shares*

On July 2, 2008, the Company's board of directors approved compensation in total of US\$300 to an independent director in exchange for her services to be provided to the Company over a three-year period commencing from July 29, 2008. The US\$300 has therefore been recognized as compensation expenses over the three-year period from July 2008 through July 2011. The initial US\$100 was paid in the form of 57,143 restricted ordinary shares of the Company in August 2008. The number of restricted ordinary shares was determined based on the closing price of the Company's ADSs on the issuance date. The remaining US\$200 was accrued as a liability and paid in cash of US\$100 in November 2009 and July 2010, respectively.

**CHINA DISTANCE EDUCATION HOLDINGS LIMITED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - continued**  
**FOR THE YEARS ENDED SEPTEMBER 30, 2009, 2010 AND 2011**  
(In thousands, except share and per share data)

**23. SHARE INCENTIVE PLAN - continued**

On December 3, 2010, the Company granted 100,000 nonvested restricted shares of the Company to directors (the “participants”) that had been outstanding at the grant date. These shares are restricted on transferability and will be forfeited if the participants cease to provide requisite service to the Company. The restriction will be removed on the first anniversary of the issuance day. The grant-date fair value of a nonvested restricted share was US\$1.25, which was the closing price of the Company’s ADSs on NYSE on December 3, 2010.

This grant results in a total share-based compensation of US\$125, which will be recognized ratably over the requisite service period of one year. As of September 30, 2011, 100,000 shares were outstanding with unrecognized compensation cost of US\$21 and with the weighted average period of 0.23 years.

A summary of the nonvested restricted shares activity is as follows:

	<u>Number of Nonvested restricted shares outstanding</u> US\$	<u>Weight average grant-date fair value</u>
Nonvested restricted shares outstanding at September 30, 2010	—	—
Granted	100,000	1.25
Forfeited	—	—
Nonvested shares outstanding at September 30, 2011	<u>100,000</u>	<u>1.25</u>

Total share-based compensation expense of share-based awards granted to employees, non-employees and non-executive directors recognized for the years ended September 30, 2009, 2010 and 2011 are as follows:

	<u>As of September 30,</u>		
	<u>2009</u> US\$	<u>2010</u> US\$	<u>2011</u> US\$
Cost of services	1,854	1,787	1,999
General and administrative expenses	1,612	2,033	3,347
Selling expenses	454	567	678
	<u>3,920</u>	<u>4,387</u>	<u>6,024</u>

**24. SUBSEQUENT EVENTS**

On November 16, 2011, the Company approved and declared a special cash dividend of \$0.12 per ordinary share on its total 135,565,361 outstanding shares as of the close of trading on December 15, 2011.

On December 5, 2011, a total amount of 7,769,168 share options was exercised, of which 6,370,868 share options were exercised at US\$0.615 per share through interest-free loans of US\$3,940 provided by the Company and the remaining 1,398,300 share options were exercised at nil. These loans are repayable upon sales of the related ordinary shares within three years or termination of employment, whichever is earlier.

**Certification by the Chief Executive Officer  
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Zhengdong Zhu, certify that:

1. I have reviewed this annual report on Form 20-F of China Distance Education Holdings 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 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 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 control over financial reporting.

Date: February 28, 2012

By: /s/ Zhengdong Zhu

Name: Zhengdong Zhu

Title: Chief Executive Officer

**Certification by the Chief Financial Officer  
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Ping Wei, certify that:

1. I have reviewed this annual report on Form 20-F of China Distance Education Holdings 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 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 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 control over financial reporting.

Date: February 28, 2012

By: /s/ Ping Wei

Name: Ping Wei

Title: Chief Financial Officer

**Certification by the Chief Executive Officer  
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, Zhengdong Zhu, Chief Executive Officer of China Distance Education Holdings Limited (the "Company"), hereby certifies, to the best of his knowledge, that the Company's annual report on Form 20-F for the year ended September 30, 2011 (the "Report") fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of, and for the periods presented in the Report.

Date: February 28, 2012

By: /s/ Zhengdong Zhu

Name: Zhengdong Zhu

Title: Chief Executive Officer

**Certification by the Chief Financial Officer  
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

Pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, Ping Wei, Chief Financial Officer of China Distance Education Holdings Limited (the “Company”), hereby certifies, to the best of her knowledge, that the Company’s annual report on Form 20-F for the year ended September 30, 2011 (the “Report”) fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934, and that the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of, and for the periods presented in the Report.

Date: February 28, 2012

By: /s/ Ping Wei

Name: Ping Wei

Title: Chief Financial Officer

**Consent of Independent Registered Public Accounting Firm**

We consent to the incorporation by reference in the Registration Statement No. 333-157129 on Form S-8 of our reports dated February 28, 2012, relating to the consolidated financial statements of China Distance Education Holdings Limited, its subsidiaries, its variable interest entity and the subsidiaries of its variable interest entity (collectively, the “Group”) and the effectiveness of the Group’s internal control over financial reporting, appearing in the Annual Report on Form 20-F of China Distance Education Holdings Limited for the year ended September 30, 2011.

/s/ Deloitte Touche Tohmatsu CPA Ltd,  
Beijing, the People’s Republic of China

February 28, 2012



February 28, 2012

China Distance Education Holdings Limited (the “**Company**”)  
18th Floor, Xueyuan International Tower  
1 Zhichun Road, Haidian District  
Beijing 100083, People’s Republic of China

Ladies and Gentlemen:

We have acted as legal advisors as to the laws of the People’s Republic of China to the Company in connection with the filing by the Company with the United States Securities and Exchange Commission of an annual report on Form 20-F for the fiscal year ended September 30, 2011 and any amendments thereto (the “Annual Report”).

We hereby consent to the use and reference to our name and our opinions and views in the Annual Report. We further consent to the filing of this letter as an exhibit to the Annual Report.

In giving such consent, we do not thereby admit that we come within the category of persons whose consent is required under Section 7 of the United States Securities Act of 1933, as amended, or the regulations promulgated thereunder.

Sincerely yours,

/s/ Jingtian & Gongcheng

\_\_\_\_\_  
Jingtian & Gongcheng

February 28, 2012

China Distance Education Holdings Limited  
18/F., Xueyuan International Tower  
No.1 Zhichun Road, Haidian District  
Beijing, China 100083

Subject: WRITTEN CONSENT OF AMERICAN APPRAISAL CHINA LIMITED

We hereby consent to the references to our name and our final appraisal reports (the “Reports”) addressed to the board of directors of China Distance Education Holdings Limited (the “Holding Company”), and to references to our valuation methodologies, assumptions and conclusions associated with such Reports, in the annual report on Form 20-F of the Holding Company and any amendments thereto (the “Annual Report”) filed or to be filed with the U.S. Securities and Exchange Commission. We further consent to the filing of this letter as an exhibit to the Annual Report.

The Reports relate to valuations of the designated assets and liabilities of a joint venture named Beijing Zhengbao Yucai Education Technology Co., Ltd. (“Zhengbao Yucai”) of which certain assets and liabilities were contributed by Beijing Yinglun Yucai Education Consulting Co., Ltd. as of March 10, 2009 and the designated assets and liabilities of a joint venture named Zhejiang Champion Xinlixiang Education Management Co., Ltd. (“Champion Xinlixiang”) of which certain assets and liabilities were contributed by Mr. Junnan Ye and Mr. Xiujie Hu from their Gaokao re-take business as of September 30, 2009 to serve the Holding Company as a basis for allocation of the purchase price to the various accounts for financial reporting purposes in accordance with U.S. GAAP. In reaching our valuation conclusions, we relied on the accuracy and completeness of the financial statements and other data provided by the Holding Company and its representatives. We did not audit or independently verify such financial statements or other data and take no responsibility for the accuracy of such information. The Holding Company determined the fair value of the above-mentioned subjects and our valuation reports were used to assist the Holding Company in reaching its determinations.

In giving such consent, we do not hereby admit that we come within the category of persons whose consent is required under Section 7 of the U.S. Securities Act of 1933, as amended, or the rules and regulations adopted by the Securities and Exchange Commission thereunder (the “Act”), nor do we admit that we are experts with respect to any part of such Annual Report within the meaning of the term “experts” as used in the Act.

Yours faithfully,

/s/ AMERICAN APPRAISAL CHINA LIMITED  
**AMERICAN APPRAISAL CHINA LIMITED**